

China Botanic Pharmaceutical  
Form 10-K  
January 30, 2012

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Form 10-K**

ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended October 31, 2011

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

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

**Commission File Number: 001-34808**

**CHINA BOTANIC PHARMACEUTICAL INC.**

*(Exact name of registrant as specified in its charter)*

Nevada 88-1273503  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

**Level 11, Changjiang International Building**

**No. 28, Changjiang Road**

**Nangang District, Harbin**

**Heilongjiang Province, China 150090**

*(Address of principal executive offices)*

**86-451-5762-0378**

*(Registrant's Telephone Number, Including Area Code)*

**Securities registered under Section 12(b) of the Act:**

Title of each class	Name of each exchange on which registered
Common Stock, \$0.001 par value	NYSE Amex LLC

**Securities registered under Section 12(g) of the Act: None**

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

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act.

Yes  No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer   
Non-accelerated filer (Do not check if a smaller reporting company)  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).   
Yes  No

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of April 29, 2011, the last business day of the registrant’s most recently completed second fiscal quarter, was approximately \$23,177,849 based upon the closing price of \$1.43 as quoted on the NYSE AMEX. Shares of common stock held by each executive officer and director and by each person who is known to own 10% or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates of the Company. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of December 31, 2011, there were 37,239,536 shares of the registrant’s \$0.001 par value common stock issued and outstanding.

No documents are incorporated into the text by reference.

**TABLE OF CONTENTS**

**PART I**

Item 1. Business	1
Item 1A. Risk Factors	19
Item 1B. Unresolved Staff Comments	33
Item 2. Properties	33
Item 3. Legal Proceedings	34
Item 4. [Removed and Reserved.]	34

**PART II**

Item 5. Market for the Registrant’s Common Stock, Related Stockholder Matters and Issuer Purchases of Equity Securities	35
Item 6. Selected Financial Data	36
Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations	36
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	47
Item 8. Financial Statements and Supplementary Data	47
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	47
Item 9A. Controls and Procedures	48
Item 9B. Other Information	49

**PART III**

Item 10. Directors, Executive Officers and Corporate Governance	50
Item 11. Executive Compensation	56
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	61
Item 13. Certain Relationships and Related Transactions, and Director Independence	63
Item 14. Principal Accountant Fees and Services	63

**PART IV**

Item 15. Exhibits and Financial Statement Schedules	64
---	----

## FORWARD LOOKING STATEMENTS

In this Annual Report on Form 10-K, references to “dollars” and “\$” are to United States dollars and, unless the context otherwise requires, references to “we,” “us” and “our” refer to China Botanic Pharmaceutical Inc. Inc. and its consolidated subsidiaries.

This Annual Report contains certain forward-looking statements. When used in this Annual Report, statements which are not historical in nature, including the words “anticipate,” “estimate,” “should,” “expect,” “believe,” “intend” “may,” “project” or “continue,” and similar expressions are intended to identify forward-looking statements. They also include statements containing anticipated business developments, a projection of revenues, earnings or losses, capital expenditures, dividends, capital structure or other financial terms.

The forward-looking statements in this Annual Report are based upon management’s beliefs, assumptions and expectations of our future operations and economic performance, taking into account the information currently available to them. These statements are not statements of historical fact. Forward-looking statements involve risks and uncertainties, some of which are not currently known to us that may cause our actual results, performance or financial condition to be materially different from the expectations of future results, performance or financial condition we express or imply in any forward-looking statements. These forward-looking statements are based on our current plans and expectations and are subject to a number of uncertainties and risks that could significantly affect current plans and expectations and our future financial condition and results.

We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this filing might not occur. We qualify any and all of our forward-looking statements entirely by these cautionary factors. As a consequence, current plans, anticipated actions and future financial conditions and results may differ from those expressed in any forward-looking statements made by or on our behalf. You are cautioned not to unduly rely on such forward-looking statements when evaluating the information presented herein.

## **PART I**

### **Item 1. *Business.***

#### **Overview**

We are a high-tech enterprise engaged in the research, development, manufacture, and distribution of botanical products, bio-pharmaceutical products, and traditional Chinese medicines, or TCM, in the People's Republic of China ("PRC" or "China"). We have three "Good Manufacturing Practice" or GMP certified production facilities - Ah City Natural and Biopharmaceutical plant, Dongfanghong pharmaceutical plant and Qingyang natural extraction plant -capable of producing 18 dosage forms and over 200 different products. Our products include but are not limited to (i) botanical anti-depression and nerve-regulation products, (ii) biopharmaceutical products, and (iii) botanical antibiotic and traditional over-the-counter ("OTC") Chinese medicines. Botanical anti-depression and nerve-regulation products account for approximately 70% of our revenues and we intend to strengthen our development in this area. We have entered into sales agency agreements with our sales agents through them our products are sold to over 3,000 distributors and over 70 sales centers across 24 provinces in China.

#### **Corporate History and Structure**

We were incorporated in the State of Nevada on August 18, 1988, originally under the corporate name of Solutions, Incorporated. We were inactive until August 16, 1996, when we changed our corporate name to Suarro Communications, Inc, and engaged in the business of providing internet based business services. In 2006 we discontinued our business operation at the time and became a non-operating public company.

On August 28, 2006, we entered into a Share Exchange Agreement (the "Exchange Agreement") with Harbin Renhuang Pharmaceutical Company Limited or Renhuang BVI, a company incorporated in the British Virgin Islands. Pursuant to the Exchange Agreement we acquired all of the outstanding capital stock of Renhuang BVI, and indirect ownership of Renhuang BVI's wholly owned subsidiary, Harbin Renhuang Pharmaceutical Co. Ltd or CBP China, which operates a pharmaceutical development, manufacturing and distribution business through various research and manufacturing facilities in the PRC.

Since our inception, we have had the following name changes:

August 1988	Solutions, Incorporated
-------------	-------------------------

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

August 1996	Suarro Communications, Inc.
June 1997	Comtech Consolidation Group, Inc.
February 1999	E-Net Corporation
May 1999	E-Net Financial Corporation
January 2000	E-Net.Com Corporation
February 2000	E-Net Financial.Com Corporation
January 2002	Anza Capital, Inc ("Anza")
July 2006	Renhuang Pharmaceuticals, Inc
November 2010	China Botanic Pharmaceutical Inc.

Substantially all of our assets and operations are located in the PRC. The following diagram illustrates our corporate structure as of October 31, 2011

China Botanic Pharmaceutical Inc. and its subsidiaries will be referred collectively as “We”, “us” or “the Company” hereinafter.

## Recent Developments

*Siberian Ginseng Polysaccharide Extract Powder.* On December 13, 2011, The Company issued a press release to announce that the company has successfully developed a new Siberian Ginseng Polysaccharide Extract Powder and was awarded the Scientific and Technological Achievements Appraisal Certificate by the Science and Technology Bureau of Heilongjiang Province. The Siberian Ginseng (Acanthopanax) Polysaccharide Extract Powder is an all-natural substance extracted from the stem of Siberian Ginseng utilizing proprietary extraction technology developed by the China Botanic research team. The Company's Extract Powder technology was developed using its patented process of separating and extracting effective parts of the Siberian Ginseng (China Patent Number: ZL200710301682X), which was granted by the State Intellectual Property Office of the People's Republic of China in December 2010. According to pharmacological research, Siberian Ginseng Extract Powder contains strong immunogenic and antitumor properties with minimal side effects. The Company's management estimates a significant market potential for Extract Powder based products, such as Siberian Ginseng Polysaccharide Extract Powder tablets and capsules. The Company plans to gradually launch its Extract Powder products in the market in 2012.

In the fourth quarter of 2011, we entered into purchase agreements with unrelated third parties to acquire the following five patents:

- Patent of Ingredients and Preparation for Parkinson Drug
- Patent of Ingredients and Preparation for XiangDouSu
- Patent of Mudouye Extract
- Patent of Hongdoushan Extract
- Patent of Ingredients and Preparation for Jizhi Pills



*Patent for “Extraction of effective ingredients of Siberian Ginseng and its preparation and application” (China Patent Number: ZL200710301682X).* In December of 2010, the Company was granted a patent by State Intellectual Property Office of PRC. The extraction method has helped the Company successfully segregate effective ingredients from Siberian Ginseng, which include three main active elements, including, Syringin, Total Glucosides and Total Flavonoids. In particular, Syringin has significant effect in the treatment of depression and nerve regulation. This patent will be a catalyst to drive the development of the Company’s innovative Acanthopanax series, such as Lyophilized Syringin Powder and Total Glucosides Total Flavonoids Soft Capsule. The patent covers a wide variety of possible Siberian Ginseng extraction methods and applications, creating a high barrier to entry for competitors seeking to develop similar Siberian Ginseng products. The patent will also provide market exclusivity for a period of 20 years.

*Ah City Phase Two project.* We have finished the architectural design of Ah City Phase Two project and are in the process of obtaining approval from relevant government authorities. We expect to finish all the procedures by April, 2012 and will start the construction once we receive approval documents. As of October 31, 2011, we have incurred a total of \$1,937,103 of construction-in-progress. The Ah City Phase Two project is expected to be completed in the year of 2013.

## Our Products

Our products mainly fall into the following three categories: (i) botanical anti-depression & nerve-regulation products, (ii) biopharmaceutical products, and (iii) botanical antibiotics and traditional OTC Chinese medicines. The table below is an illustration of our products and their main functions according to the Chinese Pharmacopeia:

Product Category	Product	Main Functions
Botanical anti-depression and nerve-regulation products	Siberian Ginseng (Acanthopanax) Series:	Antidepressant properties: Regulation of nervous excitation and inhibition; calm and inhibit spontaneous activities; improve sleep and anticonvulsant properties
	Siberian Ginseng (Acanthopanax) Tablets	
	Siberian Ginseng (Acanthopanax) Syrup	
	Siberian Ginseng (Acanthopanax) Extract(100g)	
	Siberian Ginseng (Acanthopanax) Extract(338g) [Note: The Drug Approval Number of Ginseng (Acanthopanax) Extract is under the	Improve blood properties: Improve blood flow, blood lipid profile and blood viscosity; prevent and improve cerebral thrombosis, hyperlipidemia, hypotension (low blood pressure), coronary heart disease, diabetes, leukopenia, and gonadotrophic dilation of blood vessels

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

name of Renhuang Stock\*]

*Tianma Series:*

Tianma Tablets (sugar coated, 48 tablets)

Dispel coldness; relieve pain and headache caused by blood supply shortage and blood stasis

Tianma Tablets (sugar coated, 100 tablets)

Compound Yangjiao Tablets (sugar coated, 50 tablets)

Relieve pain from migraines, vascular headaches, tension headaches and nervous headaches

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Product Category	Product	Main Functions
	Compound Schizandra Tablets	Regulation of the central nervous system. to generate body fluids and alleviate thirst, nourish the kidneys, cure insomnia and palpitations, and is also widely used as treatment for neurasthenia.
	Badger Oil	Treatment of burn and scald
Biopharmaceutical products	[Note: The Drug Approval Number of Badger Fat is under the name of Renhuang Stock*]	
	Ginseng and Venison Extract	Nourish the blood and the kidneys, restore the body's energy and increase endurance.
Botanical antibiotics and traditional OTC Chinese medicines	[Note: The Drug Approval Number of Ginseng and Venison Extract are under the name of Renhuang Stock*]	
	Banlangen Granules	Antiviral (anti-influenza) and broad-spectrum antibiotic
	Compound Honeysuckle Granules	Antiviral; antibacterial; and anti-inflammatory
	Shengmai Granules	Regulate blood flow; strengthen heart beat; and improve the immune system and blood quality
	Qing Re Jie Du Oral Liquid	Treating the flu, upper respiratory infections, and sore throats

The Siberian Ginseng (Acanthopanax) Extract, Badger Oil, and Ginseng and Venison Extract are registered by \*Renhuang Stock Co. (“Renhuang Stock”), a company of which Mr. Shaoming Li, our chairman, chief executive officer and president, serves as chairman and is a 50% shareholder. In 2010, we received licenses from Renhuang Stock to produce Siberian Ginseng (Acanthopanax) Extract.

The following table reflects the approximate sales, before sales rebates, of our three product categories during the fiscal years ended October 31, 2011 and 2010:

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Product Category	2011			2010			Change (2011 – 2010)		
	Quantity (Pack'000)	Amount (\$'000)	% of Sales	Quantity (Pack'000)	Amount (\$'000)	% of Sales	Quantity (Pack'000)	Amount (\$'000)	% of Sales
Botanical anti-depression and nerve-regulation products	489	55,789	70.1 %	529	44,697	71.3 %	(40)	11,092	24.8 %
Biopharmaceutical products	75	10,464	13.1 %	15	3,210	5.1 %	60	7,254	226.0 %
Botanical antibiotics and traditional OTC Chinese medicines	242	13,355	16.8 %	307	14,794	23.6 %	(65)	(1,439 )	(9.7 )%
Total	806	79,608	100.0%	851	62,701	100.0%	(45)	16,907	27.0 %

The following table reflects the approximate sales rebates and net sales, of our three product categories during the fiscal years ended October 31, 2011 and 2010:

Product Category	2011			2010			Change (2011-2010)		
	Sales (\$'000)	Sales rebates (\$'000)	Net sales (\$'000)	Sales (\$'000)	Sales rebates (\$'000)	Net sales (\$'000)	Sales %	Sales rebates %	Net sales %
Botanical anti-depression and nerve-regulation products	\$55,789	\$6,326	\$49,463	\$44,697	\$5,459	\$39,238	24.8 %	15.9 %	26.1 %
Biopharmaceutical products	10,464	—	10,464	3,210	1,004	2,206	226.0%	(100.0)%	374.3 %
Botanical antibiotics and traditional OTC Chinese medicines	13,355	568	12,787	14,794	1,054	13,740	(9.7 )%	(46.1 )%	(6.9 )%
Total	\$79,608	\$6,894	\$72,714	\$62,701	\$7,517	\$55,184	27.0 %	(8.3 )%	31.8 %

***Botanical anti-depression and nerve-regulation products***

Botanical anti-depression and nerve-regulation products contributed approximately \$49.46 million to our revenue in 2011 (\$39.23 million in 2010) and accounted for approximately 68.0% of total product sales after sales rebates in 2011 (71.1% in 2010).

***Siberian Ginseng (Acanthopanax):***

Acanthopanax, which is known in the United States as Siberian Ginseng, has been used for centuries in China. According to Chinese Pharmacopoeia, it has numerous medical efficacies including, improving kidney and

## Edgar Filing: China Botanic Pharmaceutical - Form 10-K

spleen function; tranquilizing the mind (anxiolytic effect), improving appetite; decreasing pain (analgesic effect); and improving sleep quality. In addition, further pharmacologic studies and clinical trials conducted over the medical efficacies of Siberian Ginseng (*Acanthopanax*) have shown additional benefits, including:

- Antidepressant

*Regulating the nervous system:* Siberian Ginseng (*Acanthopanax*) not only improves the excitation process of the central nervous system but also the inhibition process, making it more efficient. It also helps to balance the two processes to improve human intellectual and physical functions. (Source: "Chinese Medicine Information" - Microbiology Teaching and Research Section of Suzhou Medical College)

*Treating neurasthenia:* Siberian Ginseng (Acanthopanax) can significantly reduce the symptoms of neurasthenia; improves insomnia, restless sleep, heart palpitations, forgetfulness, and fatigue. (Source: “*Chinese Patent Medicine Studies, Acanthopanax Research Situation at Home and Abroad*” - Traditional Chinese Medicine Research Section of Heilongjiang Institute of Chinese Medicine)

*Treating insomnia:* Siberian Ginseng (Acanthopanax) has been proven to be effective in treating hypochondria and depression caused by insomnia and nerve dysfunction by an increasing number of scientific research departments and national institutions. There is a natural link between insomnia and depression. “Junk sleep” will lead to restlessness, low spirits and decreased work quality. Although hypochondria and depression can be attributed to external stimulus, stress and other factors, they are mainly attributed to nerve dysfunction and are classified as a psychiatric illness. (Source: “Insomnia and Depression Treatment Website” <http://www.shimianyiyu.net> )

***Treat cerebrovascular and cardiovascular disease.*** Siberian Ginseng (Acanthopanax) has positive effects on coronary heart disease, angina, high blood pressure and blood pressure regulation. (Source: “China Acanthopanax Web” <http://bjcp.xsjk.net>)

***Anti-fatigue.*** Total Glucosides of Siberian Ginseng (Acanthopanax) has powerful anti-fatigue effects that are more effective than Ginseng. (Source: “China Acanthopanax Web” <http://bjcp.xsjk.net>)

***Antioxidant.*** Siberian Ginseng (Acanthopanax) helps to delay the aging process. (Source: “China Acanthopanax Web” <http://bjcp.xsjk.net>)

***Strengthening the body:*** Total Glucosides of Siberian Ginseng (Acanthopanax) promotes fat, sugar and protein metabolism, and regeneration of hepatic (liver) cells; it improves protein and nucleic acid synthesis and strengthens physical performance. (Source: “China Acanthopanax Web” <http://bjcp.xsjk.net>)

#### *Tianma Tablets and Compound Yangjiao Tablets:*

Tianma Tablets and Compound Yangjiao Tablets are botanic drugs used to treat headaches and regulate nerves. Their known benefits and low side-effects have led to them being the top sellers among medication with similar properties in China.

#### *Compound Schisandra Tablets*

Compound Schisandra Tablets are also botanic drug which is used to regulate central nervous system, generate body fluids and alleviate thirst, nourish the kidneys, cure insomnia and palpitations, and is also widely used as treatment for neurasthenia.

***Biopharmaceutical products***

Biopharmaceutical products contributed approximately \$10.46 million to our revenue net of sales rebate in 2011 (\$3.21 million in 2010) and accounted for approximately 14.4% of total product sales net of sales rebate, in 2011 (4.0% in 2010).

### *Ginseng and Venison Extract*

Ginseng and Venison Extract comprises nutrients from ginseng and deer, and is used to nourish the blood and the kidneys, restore the body's energy and increase endurance.

### *Badger Oil*

Badger Oil expels toxin by cooling, swelling and relieving pain. For mild water and fire burns, scalds and skin pain. Promoting cells reborn and helping for improving parched, chapped and rough skin.

### ***Botanical antibiotics and traditional OTC Chinese medicine products***

Botanical antibiotics and traditional OTC Chinese medicines contributed approximately \$12.79 million to our revenue net of sales rebate in 2011 (\$13.74 million in 2010) and accounted for approximately 17.6% of total product sales net of sales rebate in 2011 (24.9% in 2010).

### **Raw materials and Suppliers**

The raw materials of Siberian Ginseng (*Acanthopanax*) based products are effective ingredients extracted from the Siberian Ginseng (*Acanthopanax*) plant. In China, about 94% of the wild Siberian Ginseng (*Acanthopanax*) resources grow in the Heilongjiang Province (Source: Heilongjiang Dongbei net). The company controlled over 75% of the wild Siberian Ginseng (*Acanthopanax*) resources production in China through exclusive purchase agreements with local governments.

On January 11, 2011, the Company through its wholly own subsidiary, CBP China, replaced and supplemented the July 8, 2010 Exclusive Purchase Agreement with Yichun Red Star Forestry Bureau of Heilongjiang Province (the "Forestry Bureau") with the Exclusive Licensing Agreement for Harbin Renhuang Pharmaceutical Co., Ltd. to Use Forest Resources under Yichun Red Star Forestry Bureau (the "Agreement") which provides us with 30 years exclusive license right to use approximately 6,667 hectares of undergrowth resources including approximately 67 hectares of Siberian Ginseng GAP cultivation base in Heilongjiang Province. We will be responsible for continued maintenance and protection of wild resources to make this area a professional Siberian Ginseng base.



In addition, through the Exclusive Purchase Agreement with Dongfanghong Forestry Bureau, we also have the exclusive rights for an indefinite term to purchase the wild Siberian Ginseng (*Acanthopanax*) grown on 6,667 hectares of land in Dongfanghong, Heilongjiang Province.

Other raw materials and packaging materials are purchased from various independent suppliers, and we do not rely on any one supplier. To ensure consistent quality, we have established long-term relationships with many of our suppliers, ensuring that we have at least ten different suppliers for each type of raw materials. We chose our suppliers based on criteria such as quality, reputation, price, delivery capacity and GMP certification. In addition, we conduct stringent inspections on each batch of raw materials supplied, and perform a periodic review of supplier qualifications.

### **Manufacturing and production facilities**

We have three production facilities: Ah City Natural and Biopharmaceutical plant, Dongfanghong pharmaceutical plant and Qingyang natural extraction plant. The facilities, with a total usable area of over 160 thousand square meters, are capable of producing more than 200 kinds of pharmaceuticals, health food, and functional food in 18 dosage forms, including tablets, capsules (hard and soft), granules, oral liquid, frozen powder injection, powder injection, liquid injection, dropping pills, and ointments. We also have  $\beta$ -lactams and plant extraction lines and automatic packaging lines.

Our production is in strict compliance with "Good Manufacturing Practice", or GMP, and Chinese standards of "Health Food Good Manufacturing Practice", and "Sterile Product Quality Control Norms". We have state of the art automated equipment, precise testing instruments, efficient air conditioning, cleaning systems and a modern logistic center for storage and distribution of products.

With the increasing demand of our products and further expansion of our business, we started Siberian Ginseng Depth Development and Industrialization Project ("Ah City Phase Two") in the beginning of 2011. We have finished the architectural design of Ah City Phase Two project and are in the process of obtaining approval documents from relevant government authorities. We expect to receive all the documents by April, 2012 and will start the construction thereafter. As of October 31, 2011, we have incurred a total of \$1,937,103 of construction-in-progress. The Ah City Phase Two project is expected to be completed in the year of 2013.

### **Quality Assurance**

We are committed to delivering high-quality pharmaceutical products, and have set in place comprehensive testing and quality control measures. We have a quality control team that carries out quality control procedures in compliance with internal policies, GMP standards and State Food and Drug Administration, or SFDA, regulations. There are quality checks at every stage of production, including testing the quality of raw materials throughout our manufacturing process, testing finished products against various criteria such as ingredient composition, weight and physical appearance, and testing sanitary conditions of the production line. We also have a pre-arranged emergency plan in the case of adverse events such as emergency plans for operational accidents and force majeure.

Our production facilities comply with pharmaceutical GMP standards. We employ automated processes and scientific parameters throughout the manufacturing process that are designed to ensure that all products meet our quality requirements. We believe that our rigorous testing and inspection procedures have been critical in ensuring that our products are quality products.

### **Marketing and Product Distribution**

We have entered into sales agency agreements with sales agents through which our products are sold to over 3,000 distributors and over 70 sales centers across 24 provinces in China. Our products are mainly sold by our distributors to pharmacies, medicine wholesale centers, hospitals and other medical agencies. No customer has contributed over 10% of our total revenue before sales rebate in fiscal year 2011 compared with one customer has contributed to 11.01% of our total revenue before sales rebate in fiscal year 2010.

Based on our product nature, distribution channel and market practices, we currently manage our sales and distribution network through four departments:

***General Business Department.*** This department is mainly responsible for distribution of botanical anti-depression and nerve-regulation products. These products are distributed to provincial distributors, who further distribute the products to local distributors. The local distributors through various sales channels, including hospitals and media marketing methods, will market the products to end consumers.

**Brand Business Department.** This department is mainly responsible for distribution of biopharmaceutical products. These products are distributed to provincial distributors, who further distribute the products to regional drugstores. The provincial distributors usually employ their own sales forces to promote the products and launch promotion campaigns with our support in marketing the products to end consumers.

**OTC Business Department.** This department is mainly responsible for distribution of botanical antibiotics and traditional OTC Chinese medicines. These products are distributed to provincial distributors, who further distribute the products to regional drugstores. The provincial distributors usually employ their own sales forces and launch their own promotion campaigns in marketing the products to end consumers.

**Allocation Business Department.** This department is responsible for bulk distribution of commonly used products. These products are distributed to medical trading centers and major market agents, who further distribute the products to nationwide drugstores and township clinics.

## **Research and Development**

We are committed to developing new products and improving our current products. During the fiscal years ended October 31, 2011 and 2010, we spent \$3,592,555 and \$3,042,815, respectively, on research and development.

Aligned with our line of business, our research and development (“R&D”) activities are focused on the following:

- Development of single-plant anti-depression & nerve regulation products;
- Extraction of certain components from Siberian Ginseng
- Cultivation of Siberian Ginseng; and
- Development of OTC product upgrades.

In 2011, we focused our research on cultivation techniques of Siberian Ginseng to solidify our future raw material supply. We are also researching on new drugs containing certain effective ingredients from Siberian Ginseng, which we expect to launch in the following years.

To further become an innovative enterprise, we continuously employ qualified talent to strengthen our research team. Currently we have established an open and innovative R&D environment consisting of Proprietary R&D Centers, Cooperation R&D Centers and Post-doctoral Workstations.

***Proprietary R&D Centers.*** These centers are responsible for initial research of potential products and development of existing product upgrades. We have comprehensive research and development facilities, including an innovative medicine division, a standard extractions division, a healthcare division, a comprehensive division, planning & registration division and a mid-phase test division. In addition, our labs have received government and industry recognitions, namely: the “Key Lab on TCM Extractions” from the Science and Technology Bureau of Heilongjiang Province and the “Innovative Medicine Lab” from the Industry Information Committee of Harbin.

**Cooperation R&D Centers.** These centers have established committees consisting of well-known medical professionals in China, who specialize in biopharmaceutical and botanical medicines. The committees guide and advise the execution and direction of R&D projects, as well as evaluating research findings. The Cooperation Centers also work closely with the academic agencies including the Institute of Biophysics and Ecological Centre of the Environment in the Chinese Academy of Science; the Medical Research Institute of National Navy; the Chinese Biochemical Medicine Research Center; the Second Army Medical University; the China Medicine University; the Beijing University of Traditional Chinese Medicine; the Heilongjiang Province Chinese Medicine University; the Northeast Forestry University and the Harbin Medical University.

**Post-doctoral Workstations.** The workstations allow post-doctoral studies on projects that are considered to be valuable to our development.

## **R&D Strategy**

Our strategy is to be the first brand and industry leader in single-plant drugs for the treatment of depression and nerve-regulation, mainly through the development of products from Siberian Ginseng (*Acanthopanax*) and Schisandra. Our goal is consistent with the following trends:

· Development of single-plant medicines is one of the three main developments in the Chinese pharmaceutical industry; and

· Antidepressants are one of the best selling drugs in the world.

To implement this strategy, we have established a cultivation base and are focusing our efforts to set the industry standard for Siberian Ginseng (*Acanthopanax*) and Schisandra products. This cultivation project has received significant support from various government departments, including the Ministry of Science and Technology, Development and Reform Commission.

## **R&D Achievements**

We have received the following achievements and recognitions for our research and development:

2011 Patent of Ingredients and Preparation for Parkinson Drug

Patent of Ingredients and Preparation for XiangDouSu

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Patent of Mudouye Extract

Patent of Hongdoushan Extract

Patent of Ingredients and Preparation for Jizhi Pills

Completed research of the chromatographic fingerprints for its Siberian Ginseng series products, utilizing a state-of-the-art analysis method which identifies the chemical characteristics of the designated medicine.

Received patent for “Extraction of effective ingredients of Siberian Ginseng and its preparation and application”,  
2010 (China Patent Number: ZL200710301682X), which was granted by the State Intellectual Property Office of the People's Republic of China in December, 2010

2009 The Siberian Ginseng (Acanthopanax) Polysaccharides products were awarded “Key Products in Heilongjiang Province” by Heilongjiang Science and Technology Office

The “Pollution-Free and Environment-Friendly Extraction Process for Total Alkaloids of *Sophora Flavescens* and Colorless Sterile Injection against Hepatitis B” project was listed as a Major Intellectual Property Rights Project by Harbin Intellectual Property Bureau.

The “Industrialization of Siberian Ginseng (*Acanthopanax*) Extraction: Total Glucosides, Total Flavonoids and Polysaccharides” project was listed as a special high-tech project by Heilongjiang Development and Reform Commission.

The “Siberian Ginseng (*Acanthopanax*) Oral liquid” project was listed as a new industrialization special project by Harbin Development and Reform Commission.

2008 The “Research on New Siberian Ginseng (*Acanthopanax*) Anti-depression Drugs” project was listed as a Harbin technological innovation talents project by Harbin Science and Technology Bureau.

2007 The “Secondary Development and Industrialization of Genuine Medical Materials Siberian Ginseng (*Acanthopanax*) Series Products” project was listed as a major provincial-level pre-project by Heilongjiang Development and Reform Commission.

### Current R&D Projects

For research and development activities, we will continue focusing on cultivation techniques of Siberian Ginseng to strengthen our future raw material supply. We also have the following four main projects under research.

***Siberian Ginseng Total Glucosides Total Flavonoids Soft Capsule.*** We are in the process of developing Siberian Ginseng Total Glucosides Total Flavonoids Soft Capsule for the treatment of senile dementia. Initial pharmacology and toxicology tests show the product to have few side effects, and are safe and reliable, and suitable for long-term use. Ongoing pharmaceutical research and evaluating quality standards and stability will last about half year. We will compile the clinical documents and apply for the clinic approval after the stage is finished. We expect to receive new drug certificate and production approval by the end of 2013 and start selling in 2014.

***Total Alkaloids of *Sophora Flavescens* Development Project.*** As a new drug against Hepatitis B, total alkaloids of *Sophora flavescens* can be used to replace - interferon, matrine and oxymatrine injections. At present, the project is in the process of pharmacology and toxicology research and which will be completed by the end of 2012. We expect to receive new drug certificate and production approval by 2015 and start selling in 2015.

***Schisandra Integrated Development Project.*** Schisandra is a wild plant with high medical and health values. Modern studies have shown that Schisandra contains lignin, which has strong efficacy in treating insomnia. The company has successfully completed the methodological work for medicinal Schisandra lignin determination and developed a sound Schisandra medicinal quality standard. At present, the project is in the process of pharmacology and toxicology test. We expect to receive new drug certificate and production approval by the end of 2015 and start selling in year 2016.



*Siberian Ginseng (Acanthopanax) Lyophilized Syringin Powder.* We have successfully segregated Syringin from Siberian Ginseng through our proprietary extraction technology. Syringin has significant effect in the treatment of depression and nerve regulation. We have created a sample of Syringin Freeze-dried Acanthopanax Powder. If successful, this achievement will represent a great pioneering work in the field of Chinese medicine, and will enhance our competitive edge in this area. We have finished pharmaceutical research. At present, the project is in the process of pharmacology and toxicology test. We plan to finish the analysis by the end of 2013 and apply for clinical trial from the State Food and Drug Administration of PRC in 2014. The new drug certificate and production approval is expected to be obtained in the end of year 2016 and start selling in 2017.

## Intellectual Property

We rely on intellectual property such as trade secrets and technical innovations, to protect and build our competitive position.

## Patents

In the fourth quarter of 2011, we entered into purchase agreements with unrelated third parties to acquire the following five patents:

- Patent of Ingredients and Preparation for Parkinson Drug
- Patent of Ingredients and Preparation for XiangDouSu
- Patent of Mudouye Extract
- Patent of Hongdoushan Extract
- Patent of Ingredients and Preparation for Jizhi Pills

We have received patent for “Extraction of effective ingredients of Siberian Ginseng and its preparation and application”, (China Patent Number: ZL200710301682X), which was granted by the State Intellectual Property Office of the People's Republic of China in December, 2011.

We have purchased from Harbin Renhuang Pharmaceutical Stock Co., Ltd (“Renhuang Stock”) two patents, Injection Preparation Method against Hepatitis B (Patent No.: ZL200410043718.5) and Total Alkaloids of Sophora Flavescens Extraction Method (Patent No.: ZL200410043717.0). Our PRC subsidiary has been registered as the owner of such patents with the Intellectual Property Office of the PRC. Renhuang Stock is a company of which Mr. Shaoming Li, our chairman, chief executive officer and president, serves as chairman and is a 50% shareholder. The patents will be

expired in 2024.

### **Design Patents**

Design patents are one of three patent categories available under Chinese patent law and are awarded to recognize a unique shape, pattern, or a combination of the two, in an industrial application. A design patent can strengthen brand value by protecting a valuable item of intellectual property. On December 20, 2009, the State Intellectual Property Office of China ("SIPO") of the People's Republic of China recently granted us patent protection for the product packaging design for its Compound Honeysuckle Granules. The patent term is 10 years. The package design of Compound Honeysuckle Granule is unique and instantly recognizable with an array of bright colors. The packaging features images of the plants which form the key ingredients of the remedies, reminding consumers that the products are all-natural, plant-based products. We now hold a total of four patents for packaging designs for Tianma Tablets, Shengmai Granules, Compound Honeysuckle Granules, and Ginseng and Venison Extract and we intend to seek patents for other proprietary designs in the future.

12

## **Trademarks**

We have received from Renhuang Stock a perpetual and non-exclusive royalty-free license to use the word “RENHUANG” in our trade name and as a trademark in connection with the sale of our products.

## **Growth Strategy**

We believe that as a result of the rapid growth of the Chinese economy, substantial increase in drug spending, aging of the population, increase in diseases related to lifestyle, government support in the pharmaceutical market and gradual application of the health insurance fund, China's pharmaceutical market will have significant potentials. In particular, we believe the demand for our products in China will increase significantly, based on the following:

### *Global market condition of depression and melancholy*

Depression has been recognized as a common mental illness. According to World Health Organization (WHO) officials, 5% of the world population is suffering from depression. In 2002, the WHO identified depression as the world's fourth largest disease and estimated that depression would be the second largest disease by 2020. What was unexpected was that depression has become the world's second largest disease (second only to cardio-cerebral vascular disease) after only 6-7 years.

According to official statistics, about 200 million Chinese were suffering from depression at the end of 2009. In the past several decades, Chinese diagnostic techniques and treating solutions of depression lagged behind western countries. Chinese people do not have adequate knowledge of this disease. At present, only about 10% of depression patients are getting medical care, far lagging behind the world treatment rate. (Source: Analysis and Prospect of China's Anti-depressant Market in 2009, edited by HDCMR.com, <http://www.hdcmr.com/> Source: Medicine Economic News, dated October 30, 2009).

Currently the eight best-selling anti-depressants in the world are: fluoxetine, paroxetine, sertraline, fluvoxamine, venlafaxine, mirtazapine, duloxetine and amitriptyline. Combined, they have 80% market share in the global anti-depression market. However, they are relatively high priced and have numerous adverse side effects. Siberian Ginseng (*Acanthopanax*) products, which are botanical medication used to treat depression and nerve-regulation, have minor side effects and are moderately priced. Therefore we believe they have significant market potential.

*Medical Reform in China*

The Chinese government announced a major comprehensive health reform effort in April 2010, committing Renminbi 850 billion over three years to the project, even amid a major economic recession. This plan has been approved by the State Council of the People's Republic of China "PRC". The implementation of this plan will give more than 90% of China's population basic health insurance policies, providing better public health and medical services.

On April 6, 2009, the State Council officially promulgated Opinions of the CPC Central Committee and the State Council on Deepening the Health Care System Reform (final version). "The Opinions" first proposed that basic medical and health institutions will be available to all the people as public products. By 2011, all urban and rural residents will have been covered by this system. The reform includes:

- ***Accelerate the building of basic medical insurance system.*** The basic medical insurances for urban workers, urban residents and the new type of rural cooperative medical care system for rural residents will cover over 90% of those eligible within three years.
- ***Establish national essential medicines system.*** All essential medicines will be listed in the reimbursement catalog of essential medicine for health insurance. To ensure essential medicine quality, the government will select a number of preferred manufacturers to be the essential medicine suppliers. The selection criteria will include but are not limited to quality, reputation, capacity, qualification, and price.
- ***Perfecting the system of health care services at grass-roots levels.*** The construction of hospitals in counties (including Chinese medicine hospitals), central health clinics in towns and townships, health care clinics in villages in remote regions and community-level medical and health institutions in underdeveloped cities will be enhanced and improved.
- ***Promote the gradual equalization of basic public health services.*** Increase in public health services and improve the funding criteria which will bring broader acceptance of Chinese medicine.
- ***Promote the reform of public hospitals.*** Hospital management system, operation and supervision mechanisms will be reformed to improve service quality of medical institutions.

Pursuant to the *Notice Concerning Releasing the State Medicine Catalogue for Basic Medical Insurance, Occupational Injury Insurance and Maternity Insurance of the PRC*, all medicines in the national essential drug list are Tier A medicines in the national medical insurance catalog; a vast majority of patients will be fully reimbursed for medicines listed in the national essential drug list. And therefore terminal sales of the listed medicines at hospitals and drug stores will be spurred. Two of our products, Banlangen Granules and Shengmai Granules, have been included in the national essential drug list. We believe we will enjoy long-term benefits from the healthcare reform as more patients could afford our products due to such full reimbursement. In addition, we expect to become one of China's essential medicine suppliers as the PRC government moves forward with its reforms in 2012.

Our growth strategy involves maximizing the opportunities that the above developments bring and capturing as much of the market share as possible in the process. To implement this strategy we plan to:

- ***Strengthen the market position of Siberian Ginseng (Acanthopanax).*** Siberian Ginseng (Acanthopanax) products have been widely recognized for their benefit in the treatment of depression and nerve-regulation. We hope

to strengthen our current market share of Siberian Ginseng (*Acanthopanax*) products by focusing on related R&D and launching new products into market. In addition, we plan to enhance sales and marketing efforts to promote the application of Siberian Ginseng (*Acanthopanax*) products as alternatives to chemical medicines used to treat depression and nerve-regulation.

- ***Expand our Siberian Ginseng (Acanthopanax) cultivating bases and adopt scientific management, gradually improving quality standards of Siberian Ginseng (Acanthopanax).*** This would enable us to be the standards-maker of Siberian Ginseng (Acanthopanax) and provide us with a competitive edge over our competitors.

- ***Reduce distribution costs through use of direct sales system:*** We intend to gradually switch the sales method of our key products from the current agency system to a direct sales system. We believe that moving to a direct sales system will reduce distribution cost and increase our profit margins. In addition, it is expected that once certain drugs become essential government procurement drugs, the sales of these drugs will also be part of our direct sales system.

## **Competition**

We face competition from pharmaceutical manufacturers producing the same type of pharmaceuticals. Our competitors vary by product categories:

### ***Botanical anti-depression and nerve-regulation products***

As a result of our low-cost access to significant wild Siberian Ginseng (Acanthopanax) resources, our advanced technology and equipment, our R&D efforts and our ability to effectively set the standard on the market, we have become the main manufacturer of these products with approximately 51% market share, which is estimated by the Company's sales department, as of fiscal year 2011. Our major competitors are Heilongjiang Gerun Pharmaceutical Co., Ltd. and Harbin Shengyuan Biological Engineering Co., Ltd. We intend to further develop this market and strengthen our leadership position.

### ***Biopharmaceutical products***

Our Ginseng and Venison Extract was introduced into the market in the fourth quarter of fiscal year 2010. To date, we believe that there is no other company produces the same product in the market.

Our Badger Oil was launched in the first quarter of fiscal year 2011. To date, we believe that there is no other company produces the same product in the market.

***Botanical Antibiotics and traditional OTC Chinese medicines***

Our Banlangen Granules have a market share of 13%, which is estimated by the Company's sales department, as of fiscal year 2011. Our major competitors are Guangzhou Baiyunshan Hutchison Whamboa Chinese Medicine Co., Ltd. and Guangzhou Xiangxue Bio-Medical Engineering Co., Ltd.

Our Compound Honeysuckle Granules have a market share of 16%, which is estimated by the Company's sales department, as of fiscal year 2011. Our major competitors are Hebei Guojin Pharmaceutical Co., Ltd. and Shiyitang Pharmaceutical Factory of Harbin Pharmaceutical Group.

Our Shengmai Granules have a market share of 5%, which is estimated by the Company's sales department, as of fiscal year 2011. Our major competitors are Hebei Meibao Pharmaceutical Co., Ltd. and Guangxi Nanjing Weiwei Pharmacy Co. Ltd.

We are aware that the main competitive factors in selling products are quality, price and product awareness. We believe that we have corresponding advantages in all of these factors.



## **Government Regulation**

Our products are subject to regulatory controls governing pharmaceutical products. As a developer, manufacturer and distributor of pharmaceuticals, we are subject to regulation and oversight by different levels of the food and drug administration in China, in particular, the PRC State Food and Drug Administration, or SFDA. The “Law of the PRC on the Administration of Pharmaceuticals,” as amended on February 28, 2001, provides the basic legal framework for the administration of the production and sale of pharmaceuticals in China and covers the manufacturing, distributing, packaging, pricing and advertising of pharmaceutical products in China. Its implementing regulations set out detailed rules with respect to the administration of pharmaceuticals in China. We believe we are in compliance with these laws and regulations in all material aspects.

Regulations at the national, provincial and local levels in China are subject to change. To date, compliance with governmental regulations has not had a material impact on our earnings or competitive position, but, because of the evolving nature of such regulations, we are unable to predict the impact such regulation may have in the foreseeable future.

## **Pharmaceutical Manufacturer**

As a manufacturer of pharmaceutical products, we are subject to continuing regulation by the SFDA. Pursuant to the PRC laws and regulations on the administration and supervision of the pharmaceutical manufacturers in the PRC, a pharmaceutical manufacturer must obtain pharmaceutical manufacturing permit from SFDA’s provincial branch. A pharmaceutical manufacturer must meet the GMP standards for each of its production facilities in the PRC in respect of each form of pharmaceutical products it produces. If a manufacturer meets the GMP standards, SFDA will issue to the manufacturer a GMP certificate with a five-year validity period. We have obtained GMP certification from SFDA to produce pharmaceutical products and raw materials in China for all of our manufacturing facilities. The GMP certification criteria include institution and staff qualifications, production premises and facilities, equipment, raw materials, hygiene conditions, production management, quality controls, product distributions, maintenance of sales records and manner of handling customer complaints and adverse reaction reports. In addition, we have obtained pharmaceutical manufacturing permits from Heilongjiang provincial food and drug administration. Our current pharmaceutical manufacturing permit, issued by the Heilongjiang branch of SFDA, will be valid until December 31, 2015.

## **Approval and Registration of Pharmaceutical Products**

A medicine must be approved and registered by the SFDA before it can be manufactured. A pharmaceutical manufacturer is allowed to manufacture a medicine only if it has obtained the medicine registration approval of such

medicine. The registration and approval process requires the manufacturer to submit to SFDA a registration application containing detailed information concerning the efficacy and quality of the medicine and the manufacturing process and the production facilities the manufacturer expects to use. The effective term of such medicine registration approval is five years and the pharmaceutical manufacturer needs to apply for and obtain the renewed medicine registration approval if it intends to continue manufacturing such medicine upon the expiration of the first five-year term. The process by SFDA for issuing and renewing the medicine registration approvals can be lengthy, and the results are unpredictable.

All of our products have received medicine registration approvals from SFDA, which approves medicine manufacturing with a national standard. Pursuant to drug approval number using agreements between Renhuang Stock and our PRC subsidiary, our PRC subsidiary is producing three products, namely Siberian Ginseng Extract, Ginseng and Venison Extract and Badger Oil, which are registered under the name of Renhuang Stock. These three products are produced in Dofanghong pharmaceutical plant, which we lease from Renhuang Stock. We have submitted applications to SFDA for the transfer of the registrations of these three products from Renhuang Stock to us. We will not be charged of any drug number using fee under the agreement before the transfer is completed. Such arrangement made by our PRC subsidiary may be deemed as producing these three products without obtaining required drug approvals before we obtain the production permission of the drugs, which may result in administrative penalties including confiscation of the inventories of these three products, confiscation of the gains arising from the manufacturing of these three products, fines, suspension of the operation and/or revocation of the Drug Production Permit of our PRC subsidiary.

### **Price Controls**

The retail prices of certain pharmaceuticals sold in China, primarily those included in the national and provincial Medical Insurance Catalogs and those pharmaceuticals whose production or trading are deemed to constitute monopolies are subject to price controls in the form of fixed prices or price ceilings. The retail prices of medicines that are subject to price controls are administered by the Price Control Office of the National Development and Reform Commission, or the NDRC, and provincial and regional price control authorities. Of our products, Siberian Ginseng Tablets, Shengmai Granules, Banlangen Granules, Compound Honeysuckle Granules, Tianma Tablets, Compound Yangjiao Tablets and Qing Re Jie Du Oral Liquid are subject to price controls. These seven products accounted for 36.2% of our total sales in fiscal year 2011.

### **Reimbursement under the National Medical Insurance Program**

The Ministry of Labor and Social Security, together with other government authorities of the PRC, determines which medicines are to be included in or removed from the national insurance medicine catalog (including Tier A and Tier B medicines) for the National Medical Insurance Program, which may affect the amounts reimbursable to program participants for their purchases of medicines. These determinations are based on a number of factors, including price and efficacy of a medicine. Although it is designated as a national program, the implementation of the National Medical Insurance Program is delegated to provincial governments, each of which has established its own medicine catalog. A provincial government must include all Tier A medicines listed in the national insurance medicine catalog in its provincial medicine catalog, but may at its sole discretion add other medicines to, or exclude Tier B medicines listed in the national insurance medicine catalog from, its provincial medicine catalog, so long as the combined numbers of the medicines added and excluded do not exceed 15% of the Tier B medicines listed in the national catalog. Depending on which Tier A or Tier B medicine is classified as in the provincial medicine catalog, a National Medical Insurance Program participant residing in that province can be reimbursed for the full cost of a Tier A medicine and for part of the cost of a Tier B medicine.

## Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Currently, four dosages of our products, including Siberian Ginseng Tablets, Shengmai Granules, Banlangen Granules and Qing Re Jie Du Oral Liquid, are included in the national catalog of the 2009 version which is currently effective and seven dosages of our products, including Siberian Ginseng Tablets, Shengmai Granules, Banlangen Granules, Compound Honeysuckle Granules, Tianma Tablets, Compound Yangjiao Tablets and Qing Re Jie Du Oral Liquid, are included in the provincial medicine catalogs of Heilongjiang province.

### **National essential drug list**

The national essential drug list is a part of the recent 2009 healthcare reform of the PRC. This new catalog is considered superior to the national medical insurance catalog because all medicines in the essential drug list are Tier A medicines in the national medical insurance catalog. Under the healthcare reform, the Chinese government proposed to establish a national basic medicine system based on a national essential drug list. According to the relevant policy, 90% of China's citizens will be covered by a universal healthcare system by the year 2012. As a result, a vast majority of patients will be fully reimbursed for medicines listed in the national essential drug list and partially reimbursed for medicines listed in the national medicine insurance catalog for the National Medical Insurance Program. Two of our products, Shengmai Granules and Banlangen Granules, have been included in the national essential drug list. We therefore believe we will enjoy long-term benefits from the healthcare reform as more patients could afford our products due to such full reimbursement. In addition, we expect that we will become one of China's essential medicine suppliers as the PRC government moves forward with its reforms in 2012.

### **Environmental Matters**

Our manufacturing facilities are subject to various pollution control regulations with respect to noise, water and air pollution and the disposal of waste and hazardous materials. We are also subject to periodic inspections by local environmental protection authorities. Our operating facilities have received certifications from the relevant PRC government agencies in charge of environmental protection indicating that the operations are in compliance with the relevant PRC environmental laws and regulations. We are not currently subject to any pending actions alleging any violations of applicable PRC environmental laws. We have obtained certification issued by the relevant local environmental protection bureau to verify Ah City plant's compliance of environmental laws.

### **Employees**

As of October 31, 2011, we have 83 full-time employees who have entered into labor contracts with our PRC subsidiary; we have approximately 485 employees dispatched from a labor dispatching company. We have approximately 142 employees in management positions, 30 in research and development, 474 in the production, storage and distribution, and 20 in the marketing and sales (excluding our 3,000 distributors in over 70 sales centers across 24 provinces in China). Our PRC subsidiary may not fully contribute the social insurance and housing fund for such 83 employees, and may not fully contribute the social insurance for the 459 dispatched employees as required by the agreement between our PRC subsidiary and the relevant employee dispatching agency.

### **Intangible Assets**

We have three patented production techniques, Injection Preparation Method against Hepatitis B (Patent No.: ZL200410043718.5), Total Alkaloids of Sophora Flavescens Extraction Method (Patent No.: ZL200410043717.0), and “Extraction of effective ingredients of Siberian Ginseng and its preparation and application”, (China Patent Number: ZL200710301682X).

In the fourth quarter of 2011, we entered into purchase agreements with unrelated third parties to acquire the following five patents:

- Patent of Ingredients and Preparation for Parkinson Drug
- Patent of Ingredients and Preparation for XiangDouSu
- Patent of Mudouye Extract
- Patent of Hongdoushan Extract
- Patent of Ingredients and Preparation for Jizhi Pills

18

We hold a total of four design patents for packaging designs for Tianma Tablets, Shengmai Granules, Compound Honeysuckle Granules, and Ginseng and Venison Extract.

On January 11, 2011, the Company through its wholly own subsidiary, CBP China, entered into an Exclusive Licensing Agreement with Yichun Red Star Forestry Bureau which provides us with an exclusive license to use approximately 6,667 hectares of undergrowth resources including approximately 67 hectares of Siberian Ginseng GAP cultivation base in Heilongjiang Province for a period of 30 years.

We have the Exclusive Purchase Agreement with Dongfanghong Forestry Bureau, through which the company has the exclusive right for an indefinite term to purchase the wild Siberian Ginseng (*Acanthopanax*) grown on 6,667 hectares of land in Dongfanghong, Heilongjiang Province.

### **Legal Proceedings**

From time to time, we may be involved in litigation relating to claims arising out of its operations in the normal course of business. Any of these claims could subject us to costly litigation and, while we generally believe that we have adequate insurance to cover many different types of liabilities, our insurance carriers may deny coverage or our policy limits may be inadequate to fully satisfy any damage awards or settlements. If this were to happen, the payment of any such awards could have a material adverse effect on our results of operations and financial position. Additionally, any such claims, whether or not successful, could damage our reputation and business. We are not a party to, or threatened by, any legal proceedings, the adverse outcome of which, in management's opinion, individually or in the aggregate, would have a material adverse effect on our results of operations or financial position.

### **Corporate Information**

Our principal executive office is located at The 11th Floor, Changjiang International Building, No. 28, Changjiang Road, Nangang District, Harbin, Heilongjiang Province, P.R. China 150090. Our telephone number at that address is 86-451-8260-2162. Our website address is [www.renhuang.com](http://www.renhuang.com). The information on our website is not a part of this Form 10-K.

### **Item 1A. Risk Factors.**

*Investment in our common stock involves risk. You should carefully consider the risks we describe below before deciding to invest. The market price of our common stock could decline due to any of these risks, in which case you could lose all or part of your investment. In assessing these risks, you should also refer to the other information included in this Annual Report, including our consolidated financial statements and the accompanying notes. You should pay particular attention to the fact that we are a holding company with substantial operations in China and are subject to legal and regulatory environments that in many respects differ from that of the United States. Our business, financial condition or results of operations could be affected materially and adversely by any of the risks discussed below and any others not foreseen. This discussion contains forward-looking statements.*

### ***Risks Related to our Business***

#### **Our products may not achieve or maintain widespread market acceptance.**

Success of our products is highly dependent on market acceptance. We believe that market acceptance of our products will depend on many factors, including:

- the perceived advantages of our products over competing products and the availability and success of competing products;



- the brand effect of our products and channel loyalty;
- the effectiveness of our sales and marketing efforts;
- the pricing and cost effectiveness of our products;
- the efficacy of our products and the prevalence and severity of adverse side effects, if any; and
- publicity concerning our products, product candidates or competing products.

If our products fail to achieve or maintain market acceptance, or if new products are introduced by others that are more favorably received than our products, are more cost effective or otherwise render our products obsolete, or if our competitors spend much more in sales and marketing efforts than we do, we may experience a decline in the demand for our products. If we are unable to market and sell our products successfully, our business, financial condition, results of operation and future growth would be adversely affected.

**Our future research and development projects may not be successful.**

The successful development of pharmaceutical products can be affected by many factors. Products that appear to be promising at their early phases of research and development may fail to be commercialized for various reasons, including the failure to obtain the necessary regulatory approvals. In addition, the research and development cycle for new products for which we may obtain an approval certificate is long.

There is no assurance that all of our future research and development projects will be successful or completed within the anticipated time frame or budget or that we will receive the necessary approvals from relevant authorities for the production of these newly developed products, or that these newly developed products will achieve commercial success. Even if such products can be successfully commercialized, they may not achieve the level of market acceptance that we expect.

**We face substantial competition in connection with the marketing and sale of our products.**

Our products compete with products with similar medical efficacy in similar market areas. Some of our competitors are well established and may have greater financial, marketing, personnel and other resources. The pharmaceutical industry is also characterized by the frequent introduction of new products. We may be unable to compete successfully or our competitors may develop products which have greater medical efficacy or gain wider market acceptance than ours.

**Our disclosure controls and procedures and our internal control over financial reporting were ineffective until recently, although we have taken remedial measures, if we are unable to effectively improve and maintain such controls and procedures, investors could lose confidence in our financial and other reports, the price of our shares of common stock may decline, and we may be subject to increased risks and liabilities.**

As a public company, we are subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, and the Sarbanes-Oxley Act of 2002. The Securities Exchange Act requires, among other things, that we file annual, quarterly and current reports with respect to our business and financial condition. Section 404 of the Sarbanes-Oxley Act requires, among other things, that we include a report of our management on our internal control over financial reporting. We are also required to include quarterly reports and certifications of our management regarding the effectiveness of our disclosure controls and procedures. In the past, our management has concluded that our disclosure controls and procedures and internal control over financial reporting were ineffective due to our late filings, and more recently, that we lack sufficient qualified accounting and financial personnel with an appropriate level of US GAAP knowledge and experience appropriate to meet our financial reporting requirements. Although we have been diligent in implementing remedial measures since the third quarter of fiscal 2009, including hiring a new chief financial officer with US GAAP and SEC reporting experience, adding additional staff, appointing three independent directors to our board of directors, engaging consultants to advise management on the preparation of Sarbanes-Oxley Section 404 compliance with internal controls over financial reporting for fiscal year 2010, there is no assurance that we will continue to have effective disclosure controls and procedures and internal control over financial reporting. If we cannot effectively and efficiently improve our controls and procedures, we could suffer material misstatements in our financial statements and other information we report and fail to meet our reporting obligations, which would likely cause investors to lose confidence in our reported financial and other information. This could lead to a decline in the trading price of our shares of common stock. Additionally, ineffective internal control over financial reporting could expose us to increased risk of fraud or misuse of corporate assets and subject us to potential delisting from NYSE Amex, regulatory investigations and civil or criminal sanctions.

**Our chairman, chief executive officer and president currently owns approximately 48% of our common stock and has the ability to prevent certain types of corporate actions, to the detriment of other stockholders.**

As of October 31, 2011, Mr. Shaoming Li, our chairman, chief executive officer and president, owns 17,850,000 shares of our common stock, which represents approximately 48% of our outstanding shares of common stock. Mr. Li is able to exercise significant influence over all matters requiring stockholder approval, including the election of a majority of the directors and determination of significant corporate actions. This concentration of ownership could also have the effect of delaying or preventing a change in control that could otherwise be beneficial to our stockholders.

**We have entered into and may continue to enter into transactions with related parties.**

We have entered into, and may continue to enter into, transactions with our related parties, including without limitation Heilongjiang Renhuang Pharmaceutical Limited and Harbin Renhuang Pharmaceutical Stock Co., Ltd. (“Renhuang Stock”), during the normal course of our business or otherwise. Mr. Shaoming Li, a major stockholder of ours and our chairman, chief executive officer and president, is a major stockholder of Heilongjiang Renhuang Pharmaceutical Limited and chairman of the board of directors and 50% stockholder of Renhuang Stock. Among others, in 2009, we entered into purchase agreements with Renhuang Stock to acquire certain real property and intellectual property for a total consideration of \$25,096,070 and \$2,456,625, respectively. The purchase prices were based on fair market value appraised by independent third party appraisal firm. Although we believe that the transactions we have entered into with Heilongjiang Renhuang Pharmaceutical Limited and Renhuang Stock are, on the whole, no more favorable, and no less favorable, than those available from unaffiliated third parties, there were no independent directors on our board at those times to approve such transactions. As such, the transactions were approved by only Mr. Shaoming Li in his capacity as our sole director. See “Certain Relationships and Related Party Transactions.” We may continue to enter into transactions with Heilongjiang Renhuang Pharmaceutical Limited and Renhuang Stock in the future.

**We may not be able to manage our expansion of operations effectively.**

We anticipate significant continued expansion of our business to address growth in demand for our products, as well as to capture new market opportunities. To manage the potential growth of our operations, we will be required to improve our operational and financial systems, procedures and controls, increase manufacturing capacity and output, expand, train and manage our growing employee base, and continuously increase our promotion budget. Furthermore, we need to maintain and expand our relationships with our customers, suppliers and other third parties. In addition, the success of our growth strategy depends on a number of internal and external factors, such as the expected growth of the pharmaceutical market in China and the competition from other pharmaceutical companies. If we are unable to manage our growth effectively, we may not be able to take advantage of market opportunities, execute our business strategies or respond to competitive pressures.

**Our future liquidity needs are uncertain and we may need to raise additional funds in the future.**

We may, from time to time, need to raise funds as part of our business operations, such as to devote financial resources to research and development of projects that we believe to have significant commercialization potential, and the acquisition or construction of manufacturing facilities. We cannot assure you that our revenues will be sufficient to meet our operational needs and capital requirements. If we need to obtain external financing, we cannot assure you that financing will be available in amounts or on terms acceptable to us, if at all. Our future liquidity needs and other business reasons could require us to sell additional equity or debt securities or obtain a credit facility. The sale of additional equity or equity-linked securities could result in additional dilution to our stockholders. The incurrence of additional indebtedness would result in increased debt service obligations and could result in operating and financing covenants that would restrict our operations.

**The retail prices of certain of our products are subject to control, including periodic adjustment, by PRC government authorities.**

Certain of our pharmaceutical products, primarily those included in the national and provincial Medical Insurance Catalogs, are subject to price controls in the form of fixed retail prices or retail price ceilings. As such, the retail prices for certain of our pharmaceutical products can be adjusted downward or upward from time to time. If the retail prices of our products are reduced by the government, our business or results of operations may be adversely affected.

Currently, of our products, Siberian Ginseng Tablets, Compound Yangjiao Tablets, Tianman Tablets, Banlangen Granules, Qing Re Jie Du Oral Liquid, Compound Honeysuckle Granules and Shengmai Granules, are subject to such price controls. These seven products accounted for 36.2% of our total sales in fiscal year 2011.

**Our results of operations may be affected by fluctuations in availability and price of raw materials.**

The raw materials we use are subject to price fluctuations due to various factors beyond our control, including, among other pertinent factors:

- increasing market demand;
- inflation;
- severe climatic and environmental conditions;
- seasonal factors, and
- changes in governmental regulations and programs.

Changes to our raw materials prices may result in increases in production and packaging costs, and we may be unable to raise the prices of our products to offset the increased costs in the short-term or at all. As a result, our results of operations may be materially and adversely affected.

**Extensive regulation of the pharmaceutical manufacturers industry in China could increase our expenses resulting in reduced profits.**

We are subject to extensive regulation by various governmental authorities in jurisdictions in which our products are manufactured or sold, regarding the processing, packaging, storage, distribution and labeling of our products. Our processing facilities and products are subject to periodic inspection by national, provincial and local authorities. We believe that we are currently in substantial compliance with all material governmental laws and regulations and maintain all permits and licenses relating to our operations.

**Clinical trials are expensive, time-consuming and difficult to design and implement.**

Clinical trials are expensive and difficult to design and implement, in part because they are subject to rigorous regulatory requirements. The clinical trial process is also time consuming, failure can occur at any stage of the trials, and we could encounter problems that cause us to abandon or repeat clinical trials. The commencement and completion of clinical trials may be delayed by several factors, including:

- unforeseen safety issues;
- determination of dosing issues;
- lack of effectiveness during clinical trials;
- slower than expected rates of patient recruitment;
- inability to monitor patients adequately during or after treatment; and
- inability or unwillingness of medical investigators to follow our clinical protocols

In addition, we (or SFDA), may suspend our clinical trials at any time if it appears that we are exposing participants to unacceptable health risks or if the regulatory bodies find serious deficiencies in our investigational new drug, submissions or the conduct of these trials. Therefore, we cannot predict with any certainty the schedule for future clinical trials.

**The results of our clinical trials may not support our product candidate claims.**

Even if our clinical trials are completed as planned, we cannot be certain that their results will support our product candidate claims. Success in pre-clinical testing and early clinical trials does not ensure that later clinical trials will be successful, and we cannot be sure that the results of later clinical trials will replicate the results of prior clinical trials and pre-clinical testing. The clinical trial process may fail to demonstrate that our product candidates are safe for humans and effective for indicated uses. This failure would cause us to abandon a product candidate and may delay

development of other product candidates.

**Physicians, patients and other end consumer may abandon existing drugs or choose not to accept and use our new drugs.**

Physicians and patients may not accept and use our products. Acceptance and use of our products will depend upon a number of factors including:

- perceptions by members of the health care community, including physicians, about the safety and effectiveness of our products;
- cost-effectiveness of our products relative to competing products; and
- effectiveness of marketing and distribution efforts by us and distributors, if any.

Because we expect sales of our current and future products to generate substantially all of our product revenues for the foreseeable future, the failure to find market acceptance would materially harm our business and results of operations.

**Our drug-development program depends upon third-party research scientists who are not subject to our control.**

We depend upon independent investigators and collaborators, such as universities and medical institutions, to conduct our pre-clinical and clinical trials under agreements with us. These collaborators are not our employees and we cannot control the amount or timing of resources that they devote to our programs. These investigators may not assign as great a priority to our programs or pursue them as diligently as we would if we were undertaking such programs ourselves. If outside collaborators fail to devote sufficient time and resources to our drug-development programs, or if their performance is substandard, the approval of our applications, and our introduction of new drugs, will be delayed. These collaborators may also have relationships with other commercial entities, some of which may compete with us. If our collaborators assist our competitors at our expense, our competitive position and business could be materially and adversely affected.

**If we cannot compete successfully for market share against other similar product oriented companies, we may not achieve sufficient product revenues and our business will suffer.**

The market for our product candidates is characterized by intense competition and rapid technological advances. We will compete with a number of existing and future drugs and therapies developed, manufactured and marketed by others. Existing or future competing products may provide greater therapeutic convenience or clinical or other benefits for a specific indication than our products, or may offer comparable performance at a lower cost. If our products fail to capture and maintain market share, we may not achieve sufficient product revenues and our business will suffer.

We will compete against fully integrated pharmaceutical companies and smaller companies that are collaborating with larger pharmaceutical companies, academic institutions, government agencies and other public and private research organizations. Many of these competitors, either alone or together with their collaborative partners, operate larger research and development programs or have substantially greater financial resources than we do, as well as significantly greater experience in:

- developing drugs;
- undertaking pre-clinical testing and human clinical trials;
- obtaining regulatory approvals of drugs;
- formulating and manufacturing drugs; and
- launching, marketing and selling drugs.



**Developments by competitors may render our products or technologies obsolete or non-competitive.**

The biotechnology and pharmaceutical industries are intensely competitive and subject to rapid and significant technological changes. A large number of companies are pursuing the development of pharmaceuticals that target the same diseases and conditions that we are targeting. We face competition from pharmaceutical and biotechnology companies in China and other countries. In addition, companies pursuing different but related fields represent substantial competition. Many of these organizations competing with us have substantially greater capital resources, larger research and development staffs and facilities, longer drug development history in obtaining regulatory approvals and greater manufacturing and marketing capabilities than we do. These organizations also compete with us to attract qualified personnel and parties for acquisitions, joint ventures or other collaborations.

**We have limited protection and are subject to substantial competition.**

We have three patented production techniques, Injection Preparation Method against Hepatitis B (Patent No.: ZL200410043718.5), Total Alkaloids of Sophora Flavescens Extraction Method (Patent No.: ZL200410043717.0), and “Extraction of effective ingredients of Siberian Ginseng and its preparation and application”, (Patent No.: ZL200710301682X). We will receive another five patents through purchase agreements made in the fourth quarter of our fiscal year 2011. Many pharmaceutical companies compete in the same market segment with similar products or products having comparable medicinal applications or therapeutic effects which may be used as direct substitutes for our products. As a result of the lack of patent protection, competitors with potential substitutes could launch similar products in the market with their prices analogous to or lower than those manufactured and sold by us. Further, the lack of patent protection could also attract an even greater number of competitors who believe they can develop products that are substantially similar to ours at a lower cost.

**If we fail to obtain or maintain applicable regulatory clearances or approvals for our products, or if such clearances or approvals are delayed, we will be unable to distribute our products in a timely manner, or at all, which could significantly disrupt our business and materially and adversely affect our sales and profitability.**

The sale and marketing of our products are subject to regulation in the PRC and in most other countries where we intend to conduct business. For a significant portion of our products, we need to obtain and renew licenses and registrations with the PRC State Food and Drug Administration, or SFDA, and its equivalent in other markets. The processes for obtaining regulatory clearances or approvals can be lengthy and expensive, and the results are unpredictable. Our PRC subsidiary is in the process of renewing the approval registrations for its products and medicines that are currently in production. Such applications have been accepted by SFDA and our PRC subsidiary is allowed by SFDA to continue to use the current drug approval numbers to manufacture its products and medicines during the application period. If we are unable to obtain clearances or approvals needed to market existing or new products, or obtain such clearances or approvals in a timely fashion, our business could be significantly disrupted and our sales and profitability could be materially and adversely affected.

In addition, our PRC subsidiary is producing three products which are registered under the name of Renhuang Stock pursuant to the agreements between Renhuang Stock and our PRC subsidiary related to the free use of drug approval numbers. We have submitted applications to SFDA for the transfer of the registrations of these three products from Renhuang Stock to us. Before the transfer is completed, such arrangement made by our PRC subsidiary may be deemed as producing these three products without obtaining required drug approvals, which may result in administrative penalties including confiscation of the inventories of these three products, confiscation of the gains arising from the manufacturing of these three products, fines, suspension of the operation and/or revocation of the Drug Production Permit of our PRC subsidiary.

In particular, as we enter foreign markets, we lack the experience and familiarity with both the regulators and the regulatory systems, which could make the process more difficult, more costly, more time consuming and less likely to succeed.

**Compliance with rules and regulations concerning corporate governance may be costly, which could harm our business.**

We will continue to incur significant legal, accounting and other expenses to comply with regulatory requirements. The Sarbanes-Oxley Act of 2002, together with rules implemented by the Securities and Exchange Commission has required and will require us to make changes in our corporate governance, public disclosure and compliance practices. Compliance with these rules and regulations has increased our legal and financial compliance costs, which have had, and may continue to have, an adverse effect on our profitability.

**We have limited insurance coverage and may incur losses resulting from product liability claims or business interruptions.**

The nature of our business exposes us to the risk of product liability claims that is inherent in the research and development, manufacturing and marketing of pharmaceutical products. These risks are greater for our products that receive regulatory approval for commercial sale. Even if a product were approved for commercial use by an appropriate governmental agency, there can be no assurance that users will not claim effects other than those intended resulted from the use of our products. While to date no material claim for personal injury resulting from allegedly defective products has been brought against us, a substantial claim or a substantial number of claims, if successful, could have a material adverse impact on our business, financial condition and results of operations.

**Compliance with rules and regulations concerning corporate governance may be costly, which could harm our business.**

We will continue to incur significant legal, accounting and other expenses to comply with regulatory requirements. The Sarbanes-Oxley Act of 2002, together with rules implemented by the Securities and Exchange Commission has required and will require us to make changes in our corporate governance, public disclosure and compliance practices. In addition, we have incurred costs and will continue to incur costs in connection with ensuring that we are in compliance with rules promulgated by the Securities and Exchange Commission regarding internal controls over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act of 2002. Compliance with these rules and regulations has increased our legal and financial compliance costs, which have had, and may continue to have, an adverse effect on our profitability.

**We are unable to assure that all of the distributors and sales centers which are selling our products have obtained the medicine supply approvals and meet the Good Supply Practice standards.**

A distributor of pharmaceutical products in China must obtain pharmaceutical distribution permit from the competent provincial or local SFDA branch. Furthermore, SFDA applies Good Supply Practice standards, or GSP standards, to all pharmaceutical wholesale and retail distributors to ensure quality of drug distribution in China.

We believe that our PRC subsidiary does not need to apply for the pharmaceutical distribution permit or GSP certification because our PRC subsidiary does not engage in the wholesale or retail of pharmaceutical manufacturer's medicines. Instead, we have entered into sales agency agreements with sales agents in 19 provinces and four municipalities, through which our products are sold to over 3,000 distributors and over 70 sales centers in China. Such distributors need to obtain the pharmaceutical distribution permit and GSP certification to sell our products. We are unable to assure that all of the distributors and sales centers which are selling our products have obtained the medicine supply approvals and meet the Good Supply Practice standards.

**We current produce our Siberian Ginseng Extract, Ginseng and Venison Extract and Badger Oil through a drug approval number using agreement with Renhuang Stock which may not be legal under the SFDA regulations.**

Pursuant to drug approval number using agreements between Renhuang Stock and our PRC subsidiary, our PRC subsidiary is producing three products, namely Siberian Ginseng Extract, Ginseng and Venison Extract and Badger Oil, which are registered under the name of Renhuang Stock. These three products are produced in Dofanghong pharmaceutical plant, which we lease from Renhuang Stock. We have submitted applications to SFDA for the transfer of the registrations of these three products from Renhuang Stock to us. However, such arrangement made by our PRC subsidiary may be deemed as producing these three products without obtaining required drug approvals before we obtain the production permission of the drugs, which may result in administrative penalties including confiscation of the inventories of these three products, confiscation of the gains arising from the manufacturing of these three products, fines, suspension of the operation and/or revocation of the Drug Production Permit of our PRC subsidiary.

**We have a limited operating history and limited historical financial information upon which you may evaluate our performance.**

We began our operations in 2006 and continue to face risks in a growth industry. We may not successfully address these risks and uncertainties or successfully implement our operating strategies. If we fail to do so, it could materially harm our business to the point of having to cease operations and could impair the value of our common stock to the point investors may lose their entire investment. Even if we accomplish these objectives, we may not generate positive cash flows or the profits we anticipate in the future.

**We rely on key executive officers and their knowledge of our business and technical expertise would be difficult to replace.**

Our success is dependent, to a large extent, on our ability to retain the services of our executive management, who have contributed to our growth and expansion to date. Our chairman, chief executive officer and president, Mr. Shaoming Li, has been, and will continue to be, instrumental to our success. Accordingly, the loss of his services, without suitable replacements, will have an adverse effect on our business generally, operating results and future prospects. We have not entered into an employment agreement with Mr. Li.

In addition, the loss of the technical knowledge and management and industry expertise of any of our key personnel could result in delays in product development, loss of customers and sales and diversion of management resources, which could adversely affect our operating results.

**Our holding company structure may hinder the payment of dividends.**

China Botanic Pharmaceutical Inc. has no direct business operations, other than its ownership of our subsidiaries. We intend to reinvest all undistributed earnings to expand our PRC operations, which the management would be most likely to benefit our shareholder. Should we decide in the future to pay dividends, as a holding company, our ability to pay dividends and meet other obligations depends upon the receipt of dividends or other payments from our operating subsidiaries and other holdings and investments. In addition, our operating subsidiaries, from time to time, may be subject to restrictions on their ability to make distributions to us due to restrictive covenants in agreements, restrictions on the conversion of local currency into U.S. dollars or other hard currency and other regulatory restrictions applicable to our subsidiaries. If future dividends are paid in Renminbi, fluctuations in the exchange rate for the conversion of Renminbi into U.S. dollars may reduce the amount received by U.S. stockholders upon conversion of the dividend payment into U.S. dollars.

A provision has not been made at October 31, 2011 for U.S. or additional foreign withholding taxes on approximately \$79,375,132 of undistributed earnings of foreign subsidiaries because it is the present intention of management to reinvest the undistributed earnings indefinitely in foreign operations.

***Risks Related to Doing Business in China***

**Our manufacturing plants are located in China and our pharmaceutical and medical products production, sale and distribution are subject to Chinese regulation.**

Economic reforms adopted by the Chinese government have had a positive effect on the economic development of the country, but the government could change these economic reforms or any of the legal systems at any time. This could either benefit or damage our operations and profitability. Some changes that could have this effect are: (i) level of government involvement in the economy; (ii) control of foreign exchange; (iii) methods of allocating resources; (iv) balance of payment positions; (v) international trade restrictions; and (vi) international conflict. Additionally, as a manufacturer of pharmaceutical and medical products located in China, we are a state-licensed company and facility and subject to Chinese regulations and laws. The Chinese government has been active in regulating the pharmaceutical industry. If we were to lose our state-licensed status we would no longer be able to manufacture pharmaceuticals in China, which is our sole operation.

**We depend upon governmental laws and regulations that may be changed in ways that will harm our business.**

Our business and products are subject to government regulations mandating the manufacturing of pharmaceuticals in China and other countries. Changes in the laws or regulations in China, or other countries we sell into, that govern or apply to our operations could have a materially adverse effect on our business. For example, the law could change so as to prohibit the use of certain pharmaceuticals. If one of our pharmaceuticals or medical products is prohibited, this change would reduce our productivity of that product.

**The Chinese government exerts substantial influence over the manner in which we must conduct our business activities.**

China only recently has permitted provincial and local economic autonomy and private economic activities. The Chinese government has exercised and continues to exercise substantial control over virtually every sector of the Chinese economy through regulation and state ownership. Our ability to operate in China may be harmed by changes in its laws and regulations, including those relating to taxation, import and export tariffs, pharmaceutical regulations,



and other matters. We believe that our operations in China are in material compliance with all applicable legal and regulatory requirements. However, the central or local governments of these jurisdictions may impose new, stricter regulations or interpretations of existing regulations that would require additional expenditures and efforts on our part to ensure our compliance with such regulations or interpretations.

Accordingly, government actions in the future, including any decision not to continue to support recent economic reforms and to return to a more centrally planned economy or regional or local variations in the implementation of economic policies, could have a significant effect on economic conditions in China or particular regions thereof, and could require us to divest ourselves of any interest we then hold in Chinese properties or joint ventures.

**The Chinese legal system may have inherent uncertainties that could materially and adversely impact our ability to enforce the agreements governing our operations.**

We are subject to oversight at the provincial and local levels of government. Our operations and prospects would be materially and adversely affected by the failure of the local government to honor our agreements or an adverse change in the laws governing them. In the event of a dispute, enforcement of these agreements could be difficult in China. China tends to issue legislation, which is followed by implementing regulations, interpretations and guidelines that can render immediate compliance difficult. Similarly, on occasion, conflicts arise between national legislation and implementation by the provinces that take time to reconcile. These factors can present difficulties in our ability to achieve compliance. Unlike the United States, China has a civil law system based on written statutes in which judicial decisions have limited precedential value. The Chinese government has enacted laws and regulations to deal with economic matters such as corporate organization and governance, foreign investment, commerce, taxation and trade. However, our experience in interpreting and enforcing our rights under these laws and regulations is limited, and our future ability to enforce commercial claims or to resolve commercial disputes in China is therefore unpredictable. These matters may be subject to the exercise of considerable discretion by agencies of the Chinese government, and forces and factors unrelated to the legal merits of a particular matter or dispute may influence their determination.

**It will be extremely difficult to acquire jurisdiction and enforce liabilities against our officers, directors and assets based in China.**

Substantially all of our assets will be located outside of the United States and most of our officers and directors will reside outside of the United States. As a result, it may not be possible for United States investors to enforce their legal rights, to effect service of process upon our directors or officers or to enforce judgments of United States courts predicated upon civil liabilities and criminal penalties of our directors and officers under Federal securities laws of the United States. Moreover, we have been advised that the PRC does not have treaties providing for the reciprocal recognition and enforcement of judgments of courts with the United States. Further, it is unclear if extradition treaties now in effect between the United States and the PRC would permit effective enforcement of criminal penalties of the Federal securities laws of the United States.

**National, provincial and local governments have established many regulations governing our business operations.**

We are also subject to numerous national, provincial and local governmental regulations, including environmental, labor, waste management, health and safety matters and product specifications and regulatory approvals from healthcare agencies. We are subject to laws and regulations governing our relationship with our employees including: wage requirements, limitations on hours worked, working and safety conditions, citizenship requirements, work permits and travel restrictions. These local labor laws and regulations may require substantial resources for compliance. Our PRC subsidiary may not fully contribute the social insurance and housing fund for the employees and the failure to do so may result in penalties and fines from PRC labor administration authorities at the provincial and local level. We are also subject to significant government regulation with regard to property ownership and use in connection with our facilities in the PRC, import restrictions, currency restrictions and restrictions on the volume of domestic sales and other areas of regulation. These regulations can limit our ability to react to market pressures in a timely or effective way, thus causing us to lose business or miss opportunities to expand our business.

**The PRC currency is not a freely convertible currency and fluctuations in the exchange rate between the PRC currency and the U.S. dollar could adversely affect our operating results.**

The PRC currency, the “Renminbi” or “RMB,” is not a freely convertible currency. We rely on the PRC government’s foreign currency conversion policies, which may change at any time, in regard to our currency exchange needs. This substantial regulation by the PRC government of foreign currency exchange may restrict our business operations and a change in any of these government policies could negatively impact our operations, which could result in a loss of profits.

The functional currency of our operations in China is the Renminbi. However, results of our operations are translated at average exchange rates into U.S. dollars for purposes of reporting results. As a result, fluctuations in exchange rates may adversely affect our expenses and results of operations as well as the value of our assets and liabilities. Fluctuations may adversely affect the comparability of period-to-period results. We do not currently use hedging techniques, and any hedging techniques which we may use in the future, may not be able to eliminate and may exacerbate the effects of currency fluctuations. Thus, exchange rate fluctuations could cause our profits, and therefore our stock prices, to decline.

**We are subject to various tax regimes, which may adversely affect our profitability and tax liabilities in the future.**

We are incorporated in the U.S. and have subsidiaries and other operations in the PRC and the British Virgin Islands. We will be subject to the tax regimes of these countries. Although virtually all of our profits will be earned outside of the U.S., under U.S. tax laws our earnings generally will be subject to U.S. taxation, because U.S. companies are generally taxed on their world-wide income. This may be true even if we do not repatriate any of its foreign earnings to the U.S. For certain types of income (generally, income from an active trade or business), U.S. companies are not required to pay tax on that income until they repatriate those earnings to the U.S. (such as for use in paying dividends or repurchasing shares). As a result, repatriation of earnings would trigger more immediate tax obligations. As a result of the imposition of U.S. taxes, our after-tax profits could decrease and could be below the level that would have been obtained if we were incorporated outside the U.S. The amount of taxes payable in the U.S. generally depends on the profitability of our various operations and the application of available tax credits and tax treaties. We are not currently receiving the benefit of any U.S. tax credit, and we are not currently conducting a material amount of business in a country with an advantageous tax treaty. Since the effect of tax credits and tax treaties depends on the profitability of operations in various jurisdictions, the amount of our tax will vary over time as we change the geographic scope of our activities. However, for the near term we expect that our total tax rate will be significantly influenced by the taxes we pay in China, so that our total tax obligation might decrease as a result of favorable tax treatment in China even though we were subject to additional U.S. taxes. In the future, we may pay significantly higher taxes than we have paid historically. In addition, any change in tax laws and regulations or the interpretation or application thereof, either internally in one of those jurisdictions or as between those jurisdictions, may adversely affect our profitability and tax liabilities in the future.

From January, 2011, our PRC subsidiary was granted a 10% tax exempt and paid 15% of enterprise income tax. Before that time, our PRC subsidiary was granted by the national tax office of Ah City a tax holiday and was fully exempt from the 25% enterprise income tax. This tax holiday was granted, without a statutory basis at the national level, by the governmental authorities of Ah City for the purposes of promoting local economic development.

**Because Chinese law governs almost all of our material agreements, we may not be able to enforce our legal rights internationally, which might result in a significant loss of business, business opportunities, or capital.**

Chinese law will govern almost all of our material agreements. We cannot assure you that we will be able to enforce any of our material agreements or that remedies will be available outside of the PRC. The system of laws and the enforcement of existing laws in the PRC may not be as certain in implementation and interpretation as in the United States. The Chinese judiciary is relatively inexperienced in enforcing corporate and commercial law, leading to a higher than usual degree of uncertainty as to the outcome of any litigation. The inability to enforce or obtain a remedy under any of our future agreements could result in a significant loss of business, business opportunities or capital.

### **Risks Related to our Securities**

**The market price of our shares is subject to significant price and volume fluctuations.**

The price of our common shares may be subject to wide fluctuations due to variations in our operating results, news announcements, our limited trading volume, general market trends both domestically and internationally, currency movements, sales of common shares by our officers, directors and our principal stockholders, and sales of common shares by existing investors. Certain events, such as the issuance of common shares upon the exercise of our outstanding stock options, could also materially and adversely affect the prevailing market price of our common shares. Further, the stock markets in general have recently experienced extreme price and volume fluctuations that have affected the market prices of equity securities of many companies and that have been unrelated or disproportionate to the operating performance of such companies. In addition, a change in sentiment by U.S. investors for China-based companies could have a negative impact on the stock price. These fluctuations may materially and adversely affect the market price of our common shares and the ability to resell shares at or above the price paid, or at any price.

**Our Articles of Incorporation authorize our board of directors to issue new series of preferred stock that may have the effect of delaying or preventing a change of control, which could adversely affect the value of your shares.**

Our articles of incorporation provide that our board of directors will be authorized to issue from time to time, without further stockholder approval, up to 1,000,000 additional shares of preferred stock in one or more series and to fix or alter the designations, preferences, rights and any qualifications, limitations or restrictions of the shares of each series, including the dividend rights, dividend rates, conversion rights, voting rights, rights of redemption, including sinking fund provisions, redemption price or prices, liquidation preferences and the number of shares constituting any series or designations of any series. Such shares of preferred stock could have preferences over our common stock with

respect to dividends and liquidation rights. We may issue additional preferred stock in ways which may delay, defer or prevent a change of control of our company without further action by our stockholders. Such shares of preferred stock may be issued with voting rights that may adversely affect the voting power of the holders of our common stock by increasing the number of outstanding shares having voting rights, and by the creation of class or series voting rights.

**We do not expect to pay dividends.**

We expect to apply our future earnings, if any, toward the further expansion and development of our business. The likelihood of us paying dividends is further reduced by the fact that, in order to pay dividends, we would need to repatriate profits earned outside of the U.S., and in doing so those profits generally would become subject to U.S. taxation. Thus, the liquidity of your investment is dependent upon your ability to sell your shares at an acceptable price, rather than receiving an income stream from your investment. The price of our stock may decline and fluctuations in market price coupled with limited trading volume in our shares may limit your ability to realize any value from your investment, including recovering the initial purchase price.

**The market price for our shares may be volatile.**

The market price for our shares is likely to be highly volatile and subject to wide fluctuations in response to factors including the following:

- actual or anticipated fluctuations in our quarterly operating results and changes or revisions of our expected results;
- changes in financial estimates by securities research analysts;
- conditions in the markets for our products;
- changes in the economic performance or market valuations of companies in our industry;
- announcements by us, or our competitors of new products, acquisitions, strategic relationships, joint ventures or capital commitments;
- addition or departure of senior management and key personnel; and
- fluctuations of exchange rates between the RMB and the U.S. dollar.

Volatility in the price of our shares may result in stockholder litigation that could in turn result in substantial costs and a diversion of our management's attention and resources.

The financial markets in the United States and other countries have experienced significant price and volume fluctuations, and market prices have been and continue to be extremely volatile. Volatility in the price of our shares may be caused by factors outside of our control and may be unrelated or disproportionate to our results of operations. In the past, following periods of volatility in the market price of a public company's securities, stockholders have frequently instituted securities class action litigation against that company. Litigation of this kind could result in substantial costs and a diversion of our management's attention and resources.



Because we do not intend to pay dividends on our shares, stockholders will benefit from an investment in our shares only if those shares appreciate in value.

We currently intend to retain all future earnings, if any, for use in the operations and expansion of the business. As a result, we do not anticipate paying cash dividends in the foreseeable future. Any future determination as to the declaration and payment of cash dividends will be at the discretion of our board of directors and will depend on factors our board of directors deems relevant, including among others, our results of operations, financial condition and cash requirements, business prospects, and the terms of our credit facilities, if any, and any other financing arrangements. Accordingly, realization of a gain on stockholders' investments will depend on the appreciation of the price of our shares, and there is no guarantee that our shares will appreciate in value.

**We may need additional capital, and the sale of additional shares or equity or debt securities could result in additional dilution to our stockholders.**

We believe that our current cash and anticipated cash flow from operations will be sufficient to meet our anticipated cash needs for the foreseeable future. As of October 31, 2011, we had cash of approximately \$15.28 million and total current assets of approximately \$51.07 million. As of October 31, 2011, we had a working capital surplus of approximately \$40.27 million. We may, however, require additional cash resources due to changed business conditions or other future developments, including any investments or acquisitions we may decide to pursue. If these resources are insufficient to satisfy our cash requirements, we may seek to sell additional equity or debt securities or obtain one or more additional credit facilities. The sale of additional equity securities could result in additional dilution to our stockholders. The incurrence of indebtedness would result in increased debt service obligations and could result in operating and financing covenants that would restrict our operations. It is uncertain whether financing will be available in amounts or on terms acceptable to us, if at all.

**Sales of a substantial number of shares of our common stock may adversely affect the market price of our common stock and the issuance of additional shares will dilute all other stockholdings.**

Sales of a substantial number of shares of our common stock in the public market, or the perception that such sales could occur, could adversely affect the market price of our common stock. Our Articles of Incorporation permits the issuance of up to approximately 100,000,000 shares of common stock, of which there are 37,239,536 outstanding as of October 31, 2011. Thus, we have the ability to issue substantial amounts of common stock in the future, which would dilute the percentage ownership held by our current stockholders.

**Item 1B. *Unresolved Staff Comments.***

Because we are not an accelerated filer, a large accelerated filer or a well-known seasoned issuer, this Item 1B is not applicable.

**Item 2. *Properties.***

We lease our Dongfanghong pharmaceutical plant located at Hulin City, Heilongjiang Province from Renhuang Stock, a company 50% owned by Mr. Shaoming Li, our chairman, chief executive officer and president. The lease has a total of approximately 3,580 square meters used for production and inventory. The lease is long term lease and we do not pay any rental fees for this.

On October 12, 2009, we entered into a purchase agreement with Harbin Renhuang Pharmaceutical Stock Co. Ltd (“Renhuang Stock”) to acquire the land use right, property and plant located at our Ah City Natural and Biopharmaceutical plant for a total consideration of \$25,096,070. The Ah City Natural and Biopharmaceutical plant is located at Harbin City, Heilongjiang Province and used for manufacturing and warehouse. Pursuant to the purchase agreement, a payment of \$15,685,044 was made to Renhuang Stock in October 2009 and a payment of \$7,842,522 was made to Renhuang Stock in January 2011, with a final payment of \$1,568,504 will be paid once we received all the related title transfer document from local government, at which time title for the assets will be transferred. According to the agreement, we were exempted from lease payments for the underlying assets starting from May 1, 2010.

Our PRC subsidiary entered into a Contract Letter dated March 3, 2007 with Yerui Pharmaceutical Co of Zhongfa Industry Group (“Yerui”), under which our PRC subsidiary may, at a consideration of RMB 3,600,000 (including repayment of a bank loan granted by Agricultural Bank of China originally borrowed by Yerui with the amount of RMB 1,090,000), acquire the properties and assets of Yerui’s Chinese traditional extraction plant. Our PRC subsidiary is currently allowed by Yerui to occupy and use the Qingyang plant without rent payment. The Qingyang plant is located at Harbin City, Heilongjiang Province and used for manufacturing and warehousing. However, our PRC subsidiary has not fully paid the bank loan on behalf of Yerui nor has the ownership of the properties of Qingyang plant been transferred to our PRC subsidiary. Additionally, the properties of Qingyang plant have been mortgaged to Agricultural Bank of China as collateral for the bank loan, and the Agricultural Bank of China will have the right to dispose of the mortgaged properties.

Our PRC subsidiary entered into a Property Purchase Contract dated April 10, 2010 with Heilongjiang Yongtai Co, which is not a related party to our Company, pursuant to which our PRC subsidiary may purchase the 10<sup>th</sup> and 11<sup>th</sup> floors of the building located at No. 28, Changjiang St., Nangang District of Harbin Municipal. Our PRC subsidiary has paid the 1<sup>st</sup> installment of the total purchase price pursuant to such Property Purchase Contract and upon the full payment of the purchase price, Heilongjiang Yongtai Co. will transfer the ownership of such property to our PRC subsidiary. The Changjiang property is used by our corporate headquarters.

In anticipation of increasing demand of our products and further expansion of our business, we started Siberian Ginseng Depth Development and Industrialization Project (“Ah City Phase Two”) in the beginning of 2011. We have finished the architectural design of Ah City Phase Two project and are in the process of obtaining approval documents from relevant government authorities. We expect to receive all the documents by April, 2012 and will start the construction thereafter. As of October 31, 2011, we have incurred a total of \$1,937,103 of construction-in-progress. The Ah City Phase Two project will be used for expanding our current Siberian Ginseng Series product production and is expected to be completed in the year of 2013.

We believe our current facilities with the ability to manufacture 18 dosage forms and over 200 products could not meet our anticipated future demand and we are building our Ah City Phase Two project to allow us to capture future market growth and demand for our products. In addition as part of our growth strategy, we may also acquire new facilities or business in the future to expand our business.

### **Item 3. *Legal Proceedings.***

From time to time, we may be involved in litigation relating to claims arising out of its operations in the normal course of business. Any of these claims could subject us to costly litigation and, while we generally believe that we have adequate insurance to cover many different types of liabilities, our insurance carriers may deny coverage or our policy limits may be inadequate to fully satisfy any damage awards or settlements. If this were to happen, the payment of any such awards could have a material adverse effect on our results of operations and financial position. Additionally, any such claims, whether or not successful, could damage our reputation and business. As of December 31, 2011, we are not a party to, or threatened by, any legal proceedings, the adverse outcome of which, in management’s opinion, individually or in the aggregate, would have a material adverse effect on our results of operations or financial position.

### **Item 4. *[Removed and Reserved.]***

**PART II****Item 5. Market for the Registrant's Common Stock, Related Stockholder Matters and Issuer Purchases of Equity Securities****Market Information**

On July 2, 2010, our common stock started trading on the NYSE Amex under the symbol "CBP." Prior to the listing on the NYSE Amex, our common stock was quoted on the Pink Sheets OTC Markets and OTC Bulletin Board. The table below lists the high and low sales price or bid price, as applicable, per share of our common stock for the respective periods as reported on the Pink Sheet OTC Market, OTC Bulletin Board or the NYSE Amex, as applicable. The following prices for each quarter during the past two fiscal years reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

	High	Low
Year Ended October 31, 2010:		
1st Quarter	\$1.18	\$0.52
2nd Quarter	\$3.00	\$1.00
3rd Quarter	\$2.79	\$1.69
4th Quarter	\$2.36	\$1.26
Year Ending October 31, 2011:		
1st Quarter	\$2.80	\$1.80
2nd Quarter	\$2.45	\$1.40
3rd Quarter	\$1.69	\$0.71
4th Quarter	\$1.42	\$0.71

On January 3, 2012, the closing sale price of our shares of common stock was \$0.80 per share and there were 37,239,536 shares of our common stock outstanding. On October 31, 2011, our shares of common stock were held by approximately 77 stockholders of record. The number of record holders was determined from the records of our transfer agent and does not include beneficial owners of our common stock whose shares are held in the names of various security brokers, dealers, and registered clearing agencies.

**Dividend Policy**

We presently do not expect to declare or pay such dividends in the foreseeable future and reinvest all undistributed earnings to expand our PRC operations, which the management would most benefit our shareholder.. Undistributed

earnings will be reinvested in our operations in PRC. Payment of dividends to our stockholders would require payment of dividends by our PRC subsidiary to us. This, in turn, would require a conversion of Renminbi into US dollars and repatriation of funds to the US. Under current PRC law, the conversion of Renminbi into foreign currency generally requires government consent. Further, government authorities may impose restrictions that could have a negative impact in the future on the conversion process or on our cash needs, which, in turn, affects our ability to pay cash dividends to our stockholders. Although our subsidiary's classification as a wholly foreign owned enterprise under PRC law permits them to declare dividends and repatriate their funds to us in the United States, any change in this status or the regulations permitting such repatriation could prevent them from doing so. Any inability to repatriate funds to us would in turn prevent payments of dividends to our stockholders.

## Item 6. Selected Financial Data

Not applicable.

## Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our audited consolidated financial statements and related notes appearing elsewhere in this Annual Report. In addition to historical financial information, the following discussion contains forward-looking statements that reflect our plans, estimates and beliefs. Our actual results could differ materially from those discussed in the forward-looking statements. Factors that could cause or contribute to these differences include those discussed below and elsewhere in this Annual Report, particularly in "Item 1A. Risk Factors."*

### Overview

We are engaged in the research, development, manufacture, and distribution of botanical products, bio-pharmaceutical products, and traditional Chinese medicines, or TCM, in the People's Republic of China. We have three GMP certified production facilities - Ah City Natural and Biopharmaceutical plant, Dongfanghong pharmaceutical plant and Qingyang natural extraction plant -capable of producing 18 dosage forms and over 200 different products. Our products include but are not limited to (i) botanical anti-depression and nerve-regulation products, (ii) biopharmaceutical products, and (iii) botanical antibiotic and traditional OTC Chinese medicines. Botanical anti-depression and nerve-regulation products account for approximate 70% of our revenues and we continue to strengthen our development in this area. We have entered into sales agency agreements with our sales agents through them our products are sold to over 3,000 distributors and over 70 sales centers across 24 provinces in China.

### Factors Affecting our Results of Operations

Our operating results are primarily affected by the following factors:

- **Pharmaceutical Industry Growth.** We believe the market for pharmaceutical products in China is growing rapidly driven by China's economic growth, increased pharmaceutical expenditure, an aging population, increased lifestyle-related diseases, government support of the pharmaceutical industry, as well as the increased availability of

funding for medical insurance in China. In particular, in January 2009, the PRC's State Council passed a far-reaching medical reform plan ("Health Reform") to help provide universal primary medical insurance coverage and increased access to medical facilities to a greater majority of its citizens. Both the central government of China and provincial governments has published Lists of Essential Medicines to regulate the market. We expect these factors to continue to drive industry growth.

**Pricing of Our Products.** Seven of our products, which accounted for 36.2% of our total revenues in fiscal year 2011, are listed on the National or Provincial List of Essential Medicines published by the Chinese government, and therefore subject to government pricing limits. We do not believe pricing controls will influence our sales significantly and expect that the health care reform will help increase our sales.



**Production Capacity.** We believe much of the pharmaceutical market in China is still underserved, particularly with respect to treatment of depression, melancholy and nerve regulation. The demand for our products that treat depression, melancholy and regulate nerves, continuously increased and we were able to increase our production of such products to capture much of this growth. We believe our current facilities with the ability to manufacture 18 dosage forms and over 200 products could not meet our future demand and we are building our Ah City Phase Two project, Depth Development and Industrialization of Siberian Ginseng, to produce more advanced Siberian Ginseng products and to allow us to capture future market growth and increase our revenue and market share accordingly.

**Perceptions of Product Quality.** We believe that rising health concerns in China have contributed to a greater demand for health-care products with perceived health benefits. We believe many consumers in China tend to prefer natural health care products with, we believe, limited side effects. Accordingly, we believe our reputation for quality and leadership position in a number of our products allow our products to command a higher average selling price and generate higher gross margins than our competitors.

**Raw Material Supply and Prices.** The per unit costs of producing our products are subject to the supply and price volatility of raw materials, which are affected by various market factors such as market demands, fluctuations in production and competition.

**Expenses Associated with Research and Development.** In order to enhance our existing products and develop new products for the market, we have devoted significant resources to R&D.

**Expenses Associated with Sales and Marketing.** In order to promote our product brand and gain greater market awareness, we have devoted significant resources to sales and marketing, in particular advertising activities.

**Demand for Our Products.** We expect the market demand for our botanic anti-depression and nerve-regulation products will increase along with the growth of the general market for such products.

## Results of Operations

The following table sets forth certain information regarding our results of operation.

	For the year ended October 31,	
	2011	2010
	(\$ in thousands)	
Statements of Operations Data		
Sales, net	72,714	55,184
Cost of goods sold	29,531	25,766
Gross profit	43,183	29,418
Operating and administrative expenses		
Sales and marketing	6,024	4,966
General and administrative	4,046	3,615
Research and development	3,593	3,043
Total operating expenses	13,663	11,624
Income from operations	29,520	17,794
Other income	127	75
Income before income tax expenses	29,647	17,869
Income tax expenses	3,728	
Net income	25,919	17,869
Other comprehensive income:		
Cumulative currency translation adjustments	3,852	1,401
Total comprehensive income	29,771	19,270

## Comparison of Years Ended October 31, 2011 and 2010

### *Total Comprehensive Income*

Total comprehensive income increased by approximately \$10.501 million, or 54.5%, from approximately \$19.27 million in 2010 to approximately \$29.77 million in 2011. This increase was primarily attributable to an increase of approximately \$17.53 million, or 31.8%, in net sales, and an increase of approximately \$3.77 million, or 14.6%, in cost of goods sold and an increase of approximately \$1.06 million, or 21.3%, in sales and marketing expenses, an increase of approximately \$0.43 million, or 11.9%, in general and administration expenses, an increase of approximately \$0.55 million, or 18.1%, in research and development expenses, and an increase of \$2.45 million in cumulative currency translation adjustments. Our gross profit margin increased from 53.3% in 2010 to 59.4% in 2011.

*Sales*

Our sales consist primarily of revenues generated from sales of Botanical anti-depression and nerve regulation products; Biopharmaceutical products and Botanical antibiotics and traditional OTC Chinese medicines. Sales increased by approximately \$17.53 million, or 31.8%, from approximately \$55.18 million in 2010 to approximately \$72.71 million in 2011. This increase in sales was primarily attributable to the launching of our new products and strong market acceptance of our Siberian Ginseng Series products as a result of our marketing efforts, in addition to the price increase of our overall products.

We provide incentive sales rebates to our sales agents. The rebate rate, which is based on a product basis, averaged of 8.7% and 12.0% of total sales for the year ended October 31, 2011 and 2010, respectively. Sales rebates are netted against total sales. The following table sets forth information regarding the net sales of our principal products before sales rebate during the fiscal years ended October 31, 2011 and 2010:

Product name	2011			2010			2011 over 2010		
	Quantity (Pack)	Amount (\$'000)	% of Sales	Quantity (Pack)	Amount (\$'000)	% of Sales	Quantity (Pack)	Amount (\$'000)	% of Sales
Siberian Ginseng (Acanthopanax) Series	356	40,939	51.4 %	388	32,208	51.4 %	-32	8,731	0.0 %
Tianma Series	50	5,448	6.8 %	59	4,780	7.6 %	-9	668	-0.8 %
Compound Yangjiao Tablets	68	7,854	9.9 %	77	7,271	11.6 %	-9	583	-1.7 %
Shark Vital Capsules	-	-	0.0 %	5	2,345	3.7 %	-5	-2,345	-3.7 %
Shengmai Granules	52	2,427	3.0 %	79	3,224	5.1 %	-27	-797	-2.1 %
Banlangen Granules	39	1,587	2.0 %	49	1,374	2.2 %	-10	213	-0.2 %
Compound Honeysuckle Granules	115	8,046	10.1 %	163	9,723	15.5 %	-48	-1,677	-5.4 %
QingReJieDu Oral Liquid	36	1,295	1.6 %	16	473	0.8 %	20	822	0.8 %
Compound Schizandra Tablets	15	1,548	1.9 %	5	438	0.7 %	10	1,110	1.2 %
Ginseng and Venison Extract	66	8,283	10.4 %	10	865	1.4 %	56	7,418	9.0 %
Badger Oil	9	2,181	2.9 %	-	-	0.0 %	9	2,181	2.9 %
Total	806	79,608	100.0 %	851	62,701	100.0 %	-45	16,907	0.0 %

While we had increased sales, we experienced a decrease in the sales of a number of our products mainly from the following few reasons. First, we increased the overall selling prices of our products range from 14.6% to 46.5% on January 1, 2011. The market normally needs six months or even longer to absorb the impact of price increase. Second, as the PRC government moves forward with the Healthcare Reform, we experienced demanding fluctuation and this situation will continue until the Healthcare Reform fully in place and the national healthcare system mature. Third, we increased the capacity per package for some of our products, such as Siberian Ginseng Tablets, the tablets per bottle increased from 100 to 400 tablets per bottle. Fourth, we focused our effort to our main products, Siberian Ginseng Series, Ginseng and Venison Extract, Badger Oil and Compound Schizandra Tablets which accounted for 66.5% of our total sales and have higher gross margin and we have dominated the market of these four products and will continue to put more effort to strengthen our market share.

The PRC government is injecting funds into healthcare insurance system to reimburse full or part of the medical expenses consumed by Chinese citizen. We expect the Healthcare Reform, when fully in place, will greatly improve the affordability of healthcare cost of Chinese people and therefore increase the demand for our products. We have established Medical Reform Sales Department as a dedicated resource focused on capturing this tremendous growth opportunity.

In the third quarter of our fiscal year 2010, we introduced two new products to the market, Qing Re Jie Du Oral Liquid, which is used to cure seasonal flu, and Compound Schisandra Tablets, also known as magnolia vine, has been clinically proven to have significant benefits to the functioning and regulation of the central nervous system. In the last quarter of our fiscal year 2010, we introduced Ginseng and Venison Extract product to the market which nourishes the blood and kidney, restores the body's energy and increase endurance and has been in great demand since we launched the product. In the first quarter of our fiscal year 2011, we introduced Badger Oil which treats burns and scalds and attracted great attention from many patients.

On January 1, 2011, we increased the average sales price per pack of our products, as demonstrated in the table below:

	2011	2010
Sales revenues before sales rebate (in thousands)	\$79,608	\$62,701
Total sales quantity (pack in thousands)	806	851
Average selling prices/pack (in thousands)	\$99	\$74

The increase in average sales price per pack, as reflected in the table, is primarily attributable to the increase in the sales price of individual products, namely Siberian Ginseng (Acanthopanax) Series, Tianma Series, Banlangen Granules and Ginseng and Venison Extract as demonstrated in the following table, which reflects the average sales price per pack by product for 2011 and 2010 and the percentage changes in the sales price per pack.

Product	Average Price Per Pack		Percentage Change	
	2011	2010	Change	%
Siberian Ginseng (Acanthopanax) Series	\$115	\$83	38.5	%
Tianma Series	109	81	34.5	%
Compound Yangjiao Tablets	116	94	23.4	%
Shark Vital Capsules	-	469	-100.0	%
Shengmai Granules	47	41	14.6	%
Banlangen Granules	41	28	46.4	%
Compound Honeysuckle Granules	70	60	16.7	%
Compound Schizandra Tablets	103	88	17.0	%
Ginseng and Venison Extract	126	86	46.5	%
Qing Re Jie Du Oral Liquid	36	30	20.0	%
Badger Oil	242	-	-	
Total	\$99	\$74	33.8	%

We expect the demand for our products will increase as we continue to garner greater market acceptance, in particular the benefits of our Siberian Ginseng (Acanthopanax) Series in treating depression and nerve-regulation. Further, we see signs of increased demand from our newly launched product, Ginseng and Venison Extract which accounted for

over 10% of our total sales revenue in fiscal year 2011. We believe that we will have a continuous and stable sales increase in these products for fiscal year 2012. In addition, we anticipate that we will be successful in becoming one of China's essential medicine suppliers as the PRC government moves forward with its Health Reforms in 2012.

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

Our costs of goods sold consist primarily of direct and indirect manufacturing costs, including raw material, packaging material, labor cost, utilities and depreciation. Cost of goods sold increased approximately \$3.77 million, or 14.6%, from approximately \$25.77 million in 2010 to approximately \$29.53 million in 2011. This increase was primarily attributable to increase in products sold and increases in certain raw material prices such as sugar and Siberian Ginseng raw material.

Although we anticipate that the cost of goods will increase due to inflationary price increases, we do not believe that such increases will be material for fiscal year 2012. We anticipate that beyond 2012, our price for raw materials and other production costs will continue to increase due to inflation. If our costs of goods increase, this may have a negative effect on our net income because due to market conditions and competitive conditions, we may not be able to increase the price for our products in proportion to the increase in costs of goods sold.

### ***Operating and Administrative Expenses***

Our total operating expenses consist primarily of sales and marketing expenses, general and administrative expenses and research and development expenses. Our total operating expenses increased by approximately \$2.04 million, or 17.5%, from approximately \$11.62 million in 2010 to approximately \$13.66 million in 2011.

*Sales and Marketing.* Our sales and marketing expenses consist primarily of advertising and market promotion expenses, and other overhead expenses incurred by the Company's sales and marketing personnel. Sales and marketing expenses increased approximately \$1.06 million, or 21.3%, from approximately \$4.97 million for 2010 to approximately \$6.02 million for 2011. This increase was primarily attributable to an increase of approximately \$0.97 million, or 20.2%, in advertising expenses as the Company intensified TV advertisements in Heilongjiang province for our botanic anti-depression series. Sales and marketing expenses are likely to increase as we continue expanding our distribution network throughout China and seek to increase our market share and awareness of our products.

*General and Administrative.* Our general and administrative expenses consist primarily of salary, travel, entertainment expenses, rental, benefits, share-based compensation, and professional service fees. General and administrative expenses increased by approximately \$0.43 million, or 11.9%, from approximately \$3.61 million for 2010 to approximately \$4.05 million for 2011. This increase was primarily attributable to an increase of approximately \$0.29 million in rental expenses, an increase of approximately \$0.13 million in amortization expenses and an increase of \$0.09 million in salary expenses. General and administrative expenses are likely to increase as we continue to expand our production, sourcing capacity, and distribution capacity throughout China.



*Research and Development.* Our research and development expenses consist primarily of salary, equipment rental expenses, and Siberian Ginseng (*Acanthopanax*) cultivation related expenses. Research and development expenses increased approximately \$0.55 million, or 18.1%, from approximately \$3.04 million for 2010 to approximately \$3.59 million for 2011. This increase was primarily attributable to development of Siberian Ginseng (*Acanthopanax*) cultivation and extraction of effective components of the Siberian Ginseng (*Acanthopanax*) plant, and development of other products, and research in cultivation techniques for Siberian Ginseng. Research and development expenses are likely to increase as we continue to devote our resources to development of new products and enhancement of our existing products.

### ***Income from Operations***

As a result of the foregoing, our income from operations increased by approximately \$11.73 million, or 65.9%, from approximately \$17.79 million in our fiscal year 2010 to approximately \$29.52 million in our fiscal year 2011.

### ***Income Tax Expenses***

We are subject to U.S. federal and state income taxes. Our subsidiary registered in the PRC is subject to enterprise income taxes in China. For the calendar years of 2011 and 2010, our PRC subsidiary was granted a tax reduction of 10% and 25%, respectively, with income tax payable of 15% and 0%, respectively. Our income tax expenses increased from \$0 for fiscal year 2010 to approximately \$3.73 million for fiscal year 2011.

### ***Cumulative Currency Translation Adjustments***

Our principal country of operations is the PRC and our functional currency is the Renminbi, but our reporting currency is the U.S. dollar. All translation adjustments resulting from the translation of our financial statements into U.S. dollars are reported as cumulative currency translation adjustments. Our cumulative currency translation adjustments increased by approximately \$2.45 million, from approximately \$1.40 million in 2010 to approximately \$3.85 million in 2011.

### **Liquidity and Capital Resources**

We had retained earnings of approximately \$53.46 million and \$79.38 million as of October 31, 2010 and 2011, respectively. As of October 31, 2011, we had cash of approximately \$15.28 million and total current assets of approximately \$51.07 million. As of October 31, 2011, we had a working capital surplus of approximately \$40.84 million. With the anticipated income from 2012, we believe our cash are adequate to satisfy our working capital needs and sustain our ongoing operations for the next twelve months.

Our summary cash flow information is as follows:

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

	Year ended October 31	
Net cash provided by (used in):	2011	2010
	(\$ in thousands)	
Operating activities	21,140	23,835
Investing activities	(34,664 )	(4,699 )

***Net Cash Provided by Operating Activities***

Net cash provided by operating activities decreased approximately \$2.70 million, from net cash provided by operating activities of approximately \$23.84 million in 2010 to net cash provided by operating activities of approximately \$21.14 million in 2011. This decrease was primarily attributable to an increase in net income of approximately \$8.05 million, an increase in the trade receivables of approximately \$4.61 million as a result of increased sales, an increase in inventories of approximately \$4.97 million, an increase in other receivables of approximately \$6.37 million and an increase in tax payable of approximately \$4.90 million.

### ***Net Cash Used in Investing Activities***

Net cash used in investing activities increased approximately \$29.97 million, from approximately \$4.70 million in 2010 to approximately \$34.66 million in 2011. This increase was primarily attributable to the increase in payments made to purchase land use right, exclusive using right of undergrowth resources, prepayment of five patents and construction in progress.

### ***Net Cash Provided by Financing Activities***

We did not have any financing activities during fiscal years ended October 31, 2011 and 2010.

### **Outstanding Long-Term Indebtedness**

None

### **Expansion Strategy**

We believe the market for pharmaceutical products in China is growing rapidly. Our growth strategy involves capturing as much of this market as possible during this rapid growth phase. To implement this strategy we plan to strengthen our dominant position in the Siberian Ginseng (Acanthopanax) market, expand our Siberian Ginseng (Acanthopanax) cultivating bases and improving the quality standards of Siberian Ginseng (Acanthopanax), and extend our distribution network through internal distribution channels reforms. Our expansion strategy will require the continued retention and investment of our earnings from operations and, we believe, additional funding from private debt and equity financing. In general, the commitment of funds to research and development, or acquisition or construction of plant and equipment tends to impair liquidity. However, we believe that because of the upward trend in our revenues in recent years, even if this trend levels off, our income from continuing operations coupled with such additional financing, if required, should provide sufficient liquidity to meet our expansion needs.

### **Off-balance Sheet Arrangements**

We do not have any off-balance sheet arrangements.

### **Contractual Obligations**

On October 12, 2009, we entered into a purchase agreement with Harbin Renhuang Pharmaceutical Stock Co. Ltd (“Renhuang Stock”) to acquire the land use right, property and plant located at our Ah City Natural and Biopharmaceutical plant for a total consideration of \$25,096,070. Pursuant to the purchase agreement, a payment of \$15,685,044 was made to Renhuang Stock in October 2009 and a payment of \$7,842,522 was made to Renhuang Stock in January 2011, with a final payment of \$1,568,504 will be paid once we received all the related title transfer document from local government, at which time title for the assets will be transferred. According to the agreement, we were exempted from lease payments for the underlying assets starting from May 1, 2010.

On April 10, 2010, CBP China entered into a Purchase Agreement with Hongxiangmingyuan of Heilongjiang Yongtai Company, to acquire two office floors for a total consideration of \$6,017,504. Pursuant to the Purchase Agreement, a payment of \$4,212,253 was made in April 2010 and recorded as deposits on the consolidated balance sheet. Pursuant to the Purchase Agreement, final payment of \$1,805,251 is due by December 20, 2012, at which time title for the assets will be transferred. Accordingly the transaction is considered incomplete as at October 31, 2011.

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Name of Fixed Asset	Purchase Date	Prepaid Amount	Remaining	
			Amount	Total Amount
		US\$	US\$	US\$
Ah City Pharmaceutical Plant	October, 2009	23,527,566	1,568,504	25,096,070
Two Office Floor	April, 2010	4,212,253	1,805,251	6,017,504
Total		27,739,819	3,373,755	31,113,574

In January, 2011, CBP China started its Ah City Phase Two project for Siberian Ginseng products development and industrialization and entered into a Construction and Engineering Design Contract (the "Contract") with Heilongjiang Medical Architecture Design Institute (the "Institute") for architectural design. A few payments have been made to Institute and relevant local government departments for design and start up fees and we recorded \$1,937,103 as Construction in progress for Ah City Phase Two project. The estimated total investment for Ah City Phase Two is \$18,822,053. In anticipation of the project proceeding, we expect to pay approximately \$9,356,129 in our fiscal year 2012 and \$7,528,821 in our fiscal year 2013. The project is anticipated to be finished in 2013.

Name of Construction in Progress	Started Date	Paid Amount	Remaining Projected Total	
			Amount	Amount
		US\$	US\$	US\$
Ah City Phase Two(Siberian Ginseng Product Industrialization)	August, 2011	1,937,103	16,884,950	18,822,053

On January 11, 2011, CBP China entered into an Exclusive Licensing Agreement for Harbin Renhuang Pharmaceutical Co., Ltd. to Use Forest Resources under Yichun Red Star Forestry Bureau (the "Agreement") with Yichun Red Star Forestry Bureau of Heilongjiang Province (the "Forestry Bureau") which provides us with 30 years exclusive license right to use approximately 6,667 hectares of undergrowth resources including approximately 67 hectares of Siberian Ginseng GAP cultivation base in Heilongjiang Province. Pursuant to the Agreement, a payment of \$7,842,522 was made to Forestry Bureau in January, 2011, second payment of \$6,274,018 was made in October, 2011 and with a final payment of \$1,568,504 due in 12 months from the date of Agreement approved by local government authorities for a total consideration of \$15,685,044. Siberian Ginseng is a plant with medically-established anti-depressant and mood regulation qualities and is also an active ingredient in our market-leading line of all-natural anti-depressant medications. We will be responsible for continued maintenance and protection of wild resources to make this area a professional Siberian Ginseng base.

In the fourth quarter of our fiscal year 2011, we purchased five patents listed as the following table.

Name of Intangible Assets	Purchase Date	Paid Amount	Remaining	Total Amount
---------------------------	---------------	-------------	-----------	--------------

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

		US\$	<b>Amount</b>	
		US\$	US\$	US\$
Patent of Ingredients and preparation for Parkinson Drug	August, 2011	1,348,914	1,348,914	2,697,828
Patent of Ingredients and preparation for XiangDousu	August, 2011	1,333,229	1,333,229	2,666,458
Patent of Mudouye Extract	September, 2011	1,882,205	1,882,205	3,764,410
Patent of Hongdoushan Extract	September, 2011	2,368,442	2,368,442	4,736,884
Patent of Ingredients and preparation for Jizhi Pills	October, 2011	2,117,481	2,117,481	4,234,962
Yichun Red Star Forrest Bureau Undergrowth Resource	January, 2011	14,116,540	1,568,504	15,685,044
Exclusive Licensing right				
Total		23,166,811	10,618,775	33,785,586

On February 1, 2011, the Company entered into an advertising contract with Harbin Weishi Advertising Company to advertise its products from February 1, 2011 to January 31, 2012 as shown on the following table.

Advertising Contract	Contract Date	Paid Amount US\$	Remaining Amount US\$	Total Amount US\$
Harbin TV Weishi Advertising Company	February, 2011	4,587,875	1,529,292	6,117,167

As of October 31, 2011, the Company has capital commitments for purchase of Ah City Nature and Pharmaceutical Plant, two office floors, undergrowth resources right, five patents, advertising contract and Ah City Phase Two construction in progress of approximately \$32,406,772. The amounts to be paid in the future years are as follows:

Calendar Year	Payment for properties
2012	\$23,072,700
2013	9,334,072
2014	
2015	
2016	
Thereafter	
Total	\$32,406,772

### Critical Accounting Policies

The consolidated financial statements include the financial statements of the Company and our subsidiaries. All transactions and balances among us and our subsidiaries have been eliminated upon consolidation.

### Accounting Judgments and Estimates

Certain amounts included in or affecting our consolidated financial statements and related disclosures must be estimated, requiring us to make certain assumptions with respect to values or conditions that cannot be known with certainty at the time the financial statements are prepared. These estimates and assumptions affect the amounts we report for assets and liabilities and our disclosure of contingent assets and liabilities at the date of our financial statements. We routinely evaluate these estimates, utilizing historical experience, consulting with experts and other methods we consider reasonable in the particular circumstances. Nevertheless, actual results may differ significantly from our estimates. Any effects on our business, financial position or results of operations resulting from revisions to



these estimates are recorded in the period in which the facts that give rise to the revision become known.

We believe that certain accounting policies are of more significance in our consolidated financial statement preparation process than others, which policies are discussed below. See also Note 2 to the consolidated financial statements for a summary of our principal accounting policies.

*Estimates of allowances for bad debts* – We must periodically review our trade and other receivables to determine if all are collectible or whether an allowance is required for possible uncollectible balances.

*Estimate of the useful lives of property and equipment* – We must estimate the useful lives and proper salvage values of our property and equipment. We must also review property and equipment for possible impairment.

*Estimate of the useful lives of intangible assets* – We must estimate the useful lives of our intangible assets. We must also review intangible assets for possible impairment.

*Inventory* – We must determine whether we have any obsolete or impaired inventory.

*Revenue recognition* – Revenue from the sale of goods is recognized on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are shipped to customers and the title has passed.

Please refer to the notes to the financial statements included elsewhere in this filing for a more complete listing of all of our critical accounting policies.

### **New Accounting Pronouncements**

In April 2011, the FASB issued ASU 2011-02 Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring. This ASU clarifies which loan modifications constitute troubled debt restructurings. It is intended to assist creditors in determining whether a modification of the terms of a receivable meets the criteria to be considered a troubled debt restructuring, both for purposes of recording an impairment loss and for disclosure of troubled debt restructurings. For public companies, this ASU is effective for interim and annual periods beginning on or after June 15, 2011, and applies retrospectively to restructurings occurring on or after the beginning of the fiscal year of adoption. Early application is permitted. It is not expected to have a material impact on the Company's consolidated financial statements.

In May 2011, the FASB issued ASU 2011-04 Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. This ASU is the result of joint efforts by the FASB and International Accounting Standards Board (“IASB”) to develop a single, converged fair value framework — that is, converged guidance on how (not when) to measure fair value and on what disclosures to provide about fair value measurements. Thus, there are few differences between this ASU and its international counterpart, IFRS 13. While this ASU is largely consistent with existing fair value measurement principles in U.S. GAAP, it expands Topic 820’s existing disclosure requirements for fair value measurements and makes other amendments. Many of these amendments were made to eliminate unnecessary wording differences between U.S. GAAP and IFRSs. However, some could change how the fair value measurement guidance in Topic 820 is applied. This ASU is effective for interim and annual periods beginning after December 15, 2011 for public entities. It is not expected to have a material impact on the Company’s consolidated financial statements.

In June 2011, the FASB issued ASU 2011-05 Comprehensive Income (Topic 220): Presentation of Comprehensive Income, which revises the manner in which entities present comprehensive income in their financial statements. This ASU removes the presentation options in Topic 220 and requires entities to report components of comprehensive income in either (1) a continuous statement of comprehensive income or (2) two separate but consecutive statements. This ASU does not change the items that must be reported in other comprehensive income. For public entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. This ASU does not require incremental disclosures in addition to those required by Topic 250 or any transition guidance. Because the Company is currently adopted to present comprehensive income within the consolidated statements of changes of equity and therefore, it is expected this ASU would change the presentation of comprehensive income in the Company's consolidated financial statements upon its adoption. It is not expected to have a material impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2011-11 Balance Sheet (Topic 210)-Disclosures about Offsetting Assets and Liabilities: The amendments in this Update will enhance disclosures required by U.S. GAAP by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45. This information will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this Update. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. It is not expected to have a material impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2011-12 Comprehensive Income (Topic 220): In order to defer only those changes in Update 2011-05 that relate to the presentation of reclassification adjustments, the paragraphs in this Update supersede certain pending paragraphs in Update 2011-05. The amendments are being made to allow the Board time to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. While the Board is considering the operational concerns about the presentation requirements for reclassification adjustments and the needs of financial statement users for additional information about reclassification adjustments, entities should continue to report 2 reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before Update 2011-05. All other requirements in Update 2011-05 are not affected by this Update, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but consecutive financial statements. Public entities should apply these requirements for fiscal years, and interim periods within those years, beginning after December 15, 2011. Nonpublic entities should begin applying these requirements for fiscal years ending after December 15, 2012, and interim and annual periods thereafter. It is not expected to have a material impact on the Company's consolidated financial statements.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

Not Applicable.

**Item 8. Financial Statements and Supplementary Data**

**Financial Statements**

Please see the accompanying Financial Statements attached hereto beginning on page F-1.

47

## **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

## **Item 9A. Controls and Procedures**

### **Evaluation of Disclosure Controls and Procedures**

As of October 31, 2011, we carried out an evaluation, under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (Exchange Act”). Accordingly, based upon that evaluation, the chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were not effective to ensure that information required to be disclosed in our periodic reports filed under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified by the Securities and Exchange Commission’s rules and regulations. Based on the management’s assessment and review of our financial statements and results for the year ended October 31, 2011, we have not established effective internal controls.

### **Management’s Report on Internal Control over Financial Reporting**

Management, under the supervision of our chief executive officer and chief financial officer, is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting (as defined in Rules 13a-15(f) and 15d(f) under the Exchange Act) is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in the United States, or GAAP. Internal control over financial reporting includes those policies and procedures that (a) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of assets, (b) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, (c) provide reasonable assurance that receipts and expenditures are being made only in accordance with appropriate authorization of management and the board of directors, and (d) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the financial statements. A “material weakness” is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the registrant’s annual or interim financial statements will not be prevented or detected on a timely basis by our internal controls. 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 the registrant's financial reporting. A "deficiency" in internal control over financial reporting 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.

During our review of our financial statements and results for the year ended October 31, 2011, our management, under the supervision and with the participation of our chief executive officer and chief financial officer, assessed the effectiveness of our internal control over financial reporting. Based on the evaluation of our internal control over financial reporting, we determined that we had significant deficiencies which could adversely affect our ability to initiate, authorize, record, process or report financial data in accordance with US GAAP. While the areas we identified are sources of potential risk, we do not believe that these potential risks have affected our financial statements or that there are any errors in our previously reported financial statements that would require restatement. The significant deficiencies we found related to a lack of sufficient qualified accounting and financing personnel with an appropriate level of US GAAP knowledge and experience appropriate to its financial reporting requirements. Based on our evaluation and because of the significant deficiencies we identified, our management concluded that our internal control over financial reporting was not effective as of October 31, 2011.

This Annual Report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act that permit us, as a smaller reporting company, to provide only management's report in this Annual Report.

### **Remediation Plan**

We are devoting significant resources to remediating, improving and documenting our disclosure controls and procedures and internal controls and procedures, and implementing additional financial and management controls, reporting systems and procedures. These measures may not ensure the adequacy of our internal controls over our financial processes and reporting in the future.

### **Changes in Internal Controls**

Since the third quarter of our 2009 fiscal year, we have begun the implementation of remedial measures including hiring of a new chief financial officer in January 2010 (who resigned on August 3, 2010 for personal reason and was replaced by an interim chief financial officer. On December 14, 2010, we subsequently hired Mr. Weiqiu Dong as our new chief financial officer), adding additional staff, appointing three independent Directors to our board of directors, engaging consultants to advise management on the preparation of Sarbanes-Oxley Section 404 compliance with internal controls over financial reporting for fiscal year 2011, providing relevant training to our staff, implementing more rigorous policies and procedures relating to period-end financial reporting and other key processes, strengthening key controls such as journal-entry approval, reconciliation procedures and maintaining relevant supporting documentation. We expect to continue to implement additional financial and management controls and procedures going forward. As results of these measures and until we have completed the remediation process, there has been and will be changes and further improvement to our internal controls over financial reporting.



**Item 9B. Other Information**

None.

49

**PART III****Item 10. Directors, Executive Officers and Corporate Governance****Directors, Executive Officers and Significant Employees**

The following table sets forth the name and age of each member of our current members of our board of directors and/or executive officers, the positions and offices held by each of them with us, and the period during which they have served in their respective position. Directors serve until the election and qualification of their successors. There was no arrangement or understanding between any executive officer or director and any other person pursuant to which any person was elected as an executive officer or director. There are no family relationships among our officers, directors, or persons nominated for such positions.

Name	Age	Position	Period Served
Shaoming Li	50	Chairman of the board of directors, Chief Executive Officer, and President	2006-present
Weiqiu Dong	41	Chief Financial Officer	2010-present
Zack Pan	44	Independent Director, Chairman of Audit Committee	2011-present(1)
Bingchun Wu	79	Independent Director, Chairman of Compensation Committee	2010-present
Changxiong Sun	67	Independent Director, Chairman of Nominations Committee	2010-present
Dianjun Pi	56	Director	2010-present
Jiang He	41	Secretary	2006-present

---

(1) Mr. Pan was appointed on October 15, 2011 by the Board of Directors.

**Shaoming Li.** Shaoming Li has served as the Chairman of the board of directors, Chief Executive Officer and President since founding Harbin Renhuang Pharmaceutical Co. Ltd. in 2006. Mr. Li has more than 20 years of experience in the pharmaceutical and finance industry. Mr. Li has been the Chairman and Chief Executive Officer of Harbin Renhuang Pharmaceutical Stock Co. Ltd since 1996. From 1984 to 1996, Mr. Li served as Vice Chairman of

Shenzhen Health Pharmaceutical Co. Ltd, a company dedicated to drug research, production, and sales. Mr. Li is a professor at Harbin Business University and Northeastern Agriculture University. Mr. Li also served as Vice Chairman of Heilongjiang Provincial Chinese Traditional Medicine Association and Heilongjiang Provincial Medicine Association. Mr. Li graduated from Central University of Finance and Economics in Beijing, China with a degree in finance.

***Wei qiu Dong.*** Wei qiu Dong was appointed to the position of Chief Financial Officer effective December 14, 2010. Prior to joining us, Mr. Dong had been the investment manager with Hatitac Inc. for 10 years, and senior audit manager with TianHua Accounting firm for 3 years. Mr. Dong holds a Bachelor of Engineering from North-Western Polytechnic University in China and is a Certified Financial Planner in Canada.

**Zack Pan.** Zack Pan was appointed to our board of director on October 15, 2011. Mr. Pan is Chairman of the Audit Committee of the board of directors. From December 30, 2009 until April 2011, Mr. Pan served as a director of Biostar Pharmaceuticals, Inc., a Chinese pharmaceutical company listed on NASDAQ (“Biostar”), and also the chairman of the board of directors’ audit committee of Biostar. Since April 2011, Mr. Pan has served as Chief Financial Officer of Biostar. Mr. Pan is a Certified Public Accountant, certified by the Oklahoma State Board of Accountancy and member of American Institute of Certified Public Accountant (AICPA). Mr. Pan was chief financial officer of China Education Alliance, Inc., a provider of quality educational resources in China, to which he was appointed in August 2009. Prior to that position, Mr. Pan was an audit manager with Eide Bailly CPAs & Business Advisors (“Eide Bailly”) at its Oklahoma City office. Mr. Pan had been working at Eide Bailly since September 2005. From September 1998 to September 2005, Mr. Pan was a statistical analyst and economist with the State of Oklahoma. From 1994 to 1996, Mr. Pan worked as a loan project officer for Asian Development Bank Loan Management Office in Anhui, China. From 1988 to 1994, Mr. Pan was an associate professor at Anhui University, China. Mr. Pan graduated with a Master of Business Administration from the University of Central Oklahoma in 1999. He obtained his Bachelor of Arts from Anhui University, China in 1988.

**Bingchun Wu.** Bingchun Wu was appointed to our board of directors in April 2010. Mr. Wu is Chairman of the Compensation Committee of the board of directors. Since 2006, Mr. Wu has served as the Team Leader of the Chinese Medicine Research Group at the Heilongjiang Province Chinese Medicine Research Institute. From 2006 to 2007, Mr. Wu served as the Chief Expert of the Chinese Medicine Group of the Innovation System of Heilongjiang Province Science and Technology Department. From 2004 to 2006, Mr. Wu served as the Director of the Chinese Pharmacology Research Office and the Head of Chinese Medicine Research at the Heilongjiang Province Science and Technology Department. Mr. Wu has a degree in Pharmaceutical Science from Shenyang Medicine University and a bachelor’s degree in financial management from Harbin University of Commerce.

**Changxiong Sun.** Changxiong Sun was appointed to our board of directors on April 2010. Mr. Sun is Chairman of the Nominations Committee of the board of directors. Since 2005, Mr. Sun has served as a Professor and Doctoral Tutor at the Management College of Harbin Institute of Technology. Since 2005 Mr. Sun has served as the Executive Director of the Overseas Development and Layout Association of China Industry, and as the Director of the Heilongjiang Dongbeiya Economy and Technology Committee. From 2004 to 2005, Mr. Sun served as the Vice Secretary General of the Harbin Municipal Government Committee. From 1999 to 2004, Mr. Sun served as the Director of the Harbin Finance Management Department. Mr. Sun has a degree in management science and engineering from the Harbin Institute of Technology.

**Dianjun Pi.** Dianjun Pi was appointed to the board of directors on April 27, 2010. Since 2004, Mr. Pi has served as our Executive Manager. From 2003 to 2004, Mr. Pi served as the Assistant General Manager of Sunflower Pharmaceuticals. From 1992 to 2003, Mr. Pi served as the Vice General Manager of China Resources Snow Breweries Co., Ltd. Mr. Pi has a post graduate degree from Renmin University of China.

**Jiang He.** Jiang He was hired as special assistant to the President in 2004 and has served as our Secretary since 2006. In this role he is in charge of asset management, risk and crisis management, and internal audit. From 2001 to 2004,

prior to joining us, he was the Vice General Manager of Heilongjiang Tiansheng High Tech Co. Ltd. In this position Mr. He was primarily responsible for managing projects, including, but not limited to, Clean Coal Projects. He received his master's degree in industrial economics in July, 2004, and his bachelor's degree in management from Jilin University in 1992.

## **Our Board of Directors**

During fiscal year 2011, our board of directors is comprised of a majority of independent directors as defined under NYSE Amex listing standards. Messrs. Pan, Sun and Wu satisfy the independence requirements established by Section 803(A)(2) of the NYSE AMEX Rules. The board of directors has determined that none of the designated independent directors have any relationship that, under NYSE Amex rules, would preclude their service on any of the standing committees of the board of directors. In making its determination, the board considered transactions and relationships between each director or his immediate family and the Company and its subsidiaries.

Mr. Pan, served as our independent director and chairman of our audit committee since October 15, 2011. Prior to that time, Mr. Xiaoheng Shao, our former director served as our independent director and chairman of our audit committee.

We are a smaller reporting company and under the NYSE AMEX Rules, we are only required to maintain a Board comprising of directors at least half of which are independent directors, and an audit committee of at least two members, comprised solely of independent directors who also meet the requirements of Rule 10A-3 under the Securities Exchange Act of 1934, as amended (“Exchange Act”).

We have the following board committees: Audit Committee, Compensation Committee and Nominations Committee. Each Board Committee consists entirely of independent and non-employee directors. The Board has adopted a written charter for each of the committees which is available on the Company’s website [www.renhuang.com](http://www.renhuang.com). Printed copies of each of our committee charter may be obtained, without charge, by contacting the corporate secretary, China Botanic Pharmaceutical Inc., Level 11, Changjiang International Building, No. 28, Changjiang Road, Nangang District, Harbin, Heilongjiang Province, China 150090.

## **Board Leadership Board’s Role in Risk Oversight**

Our chairman of the board of director and chief executive officer is Mr. Li. During fiscal year 2011, the majority of directors are independent and our Audit Committee, Compensation Committee and Nominating Committee are comprised entirely of independent directors. We do not have a lead independent director. Audit Committee is responsible for oversight of risks relating to our accounting matters, financial reporting and legal and regulatory compliance. To satisfy these oversight responsibilities, the Audit Committee meets with management, our internal auditor and independent registered public accounting firm. The Compensation Committee is responsible for overseeing risks relating to employment policies and our policies on structuring compensation programs. To satisfy these oversight responsibilities, the Compensation Committee intends to meet regularly with management to understand the implications of compensation decisions, and particularly risks our compensation policies pose to our

finances, human resources and stockholders.

### **Meetings of the Board of Directors**

During the fiscal year 2011, our board took action by unanimous board of director consents 1 time and held 1 meeting. During the fiscal year 2011, our audit committee held 4 meetings and took action by written consent 1 time, and our nominating committee did not hold a meeting in fiscal year 2011. We do not have a policy with regard to Board members' attendance at annual meetings of stockholders. All directors with the exception of Mr. Xiaoheng Shao attended our 2010 Annual Meeting of Stockholders.

### **Audit Committee**

Our board of directors has established an Audit Committee in accordance with section 3(a)(58)(A) of the Exchange Act which, during fiscal year 2011, consists of the following independent directors: Messrs. Pan, Sun and Wu. Mr. Pan, served as our independent director and chairman of our audit committee since October 15, 2011. Prior to that time, Mr. Xiaoheng Shao, our former director served as our independent director and chairman of our audit committee.

Each member of the Audit Committee meets the independence criteria prescribed by Rule 10A-3 under the Exchange Act, and each constitutes an “independent director” as defined in Section 803(A)(2) of the NYSE AMEX Rules.

The primary purpose of the Audit Committee is to oversee our accounting and financial reporting processes and the function of the Audit Committee includes retaining our independent auditors, reviewing their independence standards, reviewing and approving the planned scope of our annual audit, reviewing and approving any fee arrangements with our auditors, overseeing their audit work, reviewing and pre-approving any non-audit services that may be performed by them, reviewing the adequacy of accounting and financial controls, reviewing our critical accounting policies and reviewing and approving any related party transactions.

### **Audit Committee Financial Expert**

On October 15, 2011, Mr. Pan was appointed as the chairman of audit committee of our board of directors and served as the chairman of our audit committee. From December 30, 2009 until April 2011, Mr. Pan served as a director of Biostar Pharmaceuticals, Inc., a Chinese pharmaceutical company listed on NASDAQ (“Biostar”), and also the chairman of the board of directors’ audit committee of Biostar. Since April 2011, Mr. Pan has served as Chief Financial Officer of Biostar. Mr. Pan is a Certified Public Accountant, certified by the Oklahoma State Board of Accountancy and member of American Institute of Certified Public Accountant (AICPA). Mr. Pan was chief financial officer of China Education Alliance, Inc., a provider of quality educational resources in China, to which he was appointed in August 2009. Prior to that position, Mr. Pan was an audit manager with Eide Bailly CPAs & Business Advisors (“Eide Bailly”) at its Oklahoma City office. Mr. Pan had been working at Eide Bailly since September 2005. During his term with the Company, Mr. Pan’s extensive finance, industry, and CFO experience provides our Board with a valuable resource in understanding company operations and evaluating strategic opportunities. During fiscal year ended October 31, 2011, the Board has determined that Mr. Pan is the “audit committee financial expert” as such term is defined in Item 407(d) of Regulation S-K promulgated by the SEC.

### **Other Board Committees**



Our board of directors has two additional board committees: the Compensation Committee and the Nominations Committee. The members of our Compensation Committee and Nominations Committee are comprised of the following independent directors: Messrs. Pan, Wu and Shao. The Nomination Committee held 1 meeting during fiscal year 2011. The Compensation Committee did not hold a meeting in fiscal year 2011.

## **Compensation Committee**

Our Compensation Committee assists the Board in discharging the Board's responsibilities relating to management organization, performance, compensation and succession. The Compensation Committee is permitted to delegate its authority in accordance with Nevada law unless prohibited by the Company's bylaws or the Compensation Committee charter. In discharging its responsibilities, the Compensation Committee shall, amongst other things:

- ◆ Consider and authorize the compensation philosophy for the Company's personnel.
- ◆ Review and approve corporate goals and objectives relevant to chief executive officer and senior management compensation, evaluate chief executive officer and senior management performance in light of those goals and objectives and, either as a committee or together with other independent directors (as directed by the Board of Directors), determine and approve chief executive officer and senior management compensation based on this evaluation.
- ◆ Annually review and approve perquisites for the chief executive officer and senior management.
- ◆ Make recommendations to the Board of Directors with respect to the Company's employee benefit plans.
- ◆ Administer incentive, deferred compensation and equity based plans.
- ◆ Annually review and update this Charter for consideration by the Board of Directors.
- ◆ Annually evaluate performance and function of the Compensation Committee.
- ◆ Report the matters considered and actions taken by the Compensation Committee to the Board of Directors.

## **Compensation Committee Interlocks and Insider Participation**

All current members of the Compensation Committee are independent directors, and all past members were independent directors at all times during their service on such Committee. None of the past or present members of our Compensation Committee are present or past employees or officers of ours or any of our subsidiaries. No member of the Compensation Committee has had any relationship with us requiring disclosure under Item 404 of Regulation S-K. None of our executive officers serves on the board of directors or compensation committee of a company that has an executive officer that serves on our Board or compensation committee.

## **Nominations Committee**

The Nominations Committee assists the Board in identifying individuals qualified to become our directors and in determining the composition of the Board and its committees. The Nominations Committee is responsible for, among other things:

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

- Make recommendations to the Board with respect to the size and composition of the Board;
- Make recommendations to the Board on the minimum qualifications and standards for director nominees and the selection criteria for the Board members, and
- Review the qualifications of potential candidates for the Board;
- Make recommendations to the Board on nominees to be elected at the Annual Meeting of Stockholders; and
- Seek and identify a qualified director nominee, in the event that a director vacancy occurs, to be recommended to the Board for either appointment by the Board to serve the remainder of the term of a director position that is vacant or election at the Annual Meeting of the Stockholders.

### **Code of Ethics**

We have adopted a Code of Ethics. It is available on our website, located at <http://www.renhuang.com>

### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our executive officers and directors and persons who own more than 10% of a registered class of our equity securities, to file with the Securities and Exchange Commission (hereinafter referred to as the “Commission”) initial statements of beneficial ownership, reports of changes in ownership and Annual Reports concerning their ownership, of Common Stock and other of our equity securities on Forms 3, 4, and 5, respectively. Executive officers, directors and greater than 10% shareholders are required by Commission regulations to furnish us with copies of all Section 16(a) reports they file.

To the best of our knowledge, based solely on information publicly available, during the fiscal year ended October 31, 2011, all of our directors and executive officers complied with Section 16(a) filing requirements.

### **Involvement in Certain Legal Proceedings**

None of our directors, executive officers or control persons has been involved in any of the events described in Rule 401(f) of Regulation S-K in the last 10 years.

**Item 11. Executive Compensation****Summary Compensation Table**

Our Compensation Committee, which currently consists of Messrs. Shaoming Li, Zack ZiBing Pan and Bingchun Wu, assists our board of directors in reviewing and approving the compensation structure of our directors and executive officers, including all forms of compensation to be provided to our directors and executive officers. With the responsibility of establishing, implementing and monitoring our executive compensation program philosophy and practices, our Compensation Committee seeks to ensure that the total compensation paid to our directors and executive officers is fair and competitive.

The following table sets forth information regarding all forms of compensation received by all persons who served as our Principal Executive Officer and Principal Financial Officer during the fiscal years ended October 31, 2011 and 2010, respectively. We did not have any executive officer who received more than \$100,000 for services during the fiscal years ended October 31, 2011 and 2010, respectively.

Name and Principal Position (a)	Year (b)	Salary (c)	Bonus (d)	Stock Awards (e) <sup>(1)</sup>	Option Awards (f) <sup>(1)</sup>	All Other Compensation (g)	Total (h)
Shaoming Li, Chairman of Board of Directors, Chief Executive Officer, and President	2011	\$31,250	\$ -0-	\$ -0-	\$-0-	\$ -0-	\$31,250
	2010	\$31,250	\$ -0-	\$ -0-	\$-0-	\$ -0-	\$31,250
Weiqiu Dong, Chief Financial Officer <sup>(2)</sup>	2011	\$91,993	\$ -0-	\$ -0-	\$259,251 <sup>(2)</sup>	\$ -0-	\$351,2444
	2010	\$-	\$ -	\$ -	\$-	\$ -	\$-
Xiaoying Lu, Former Interim Chief Financial Officer <sup>(3)</sup>	2011	\$7,051	\$ -0-	\$ -0-	\$-0-	\$ -0-	\$7,051
	2010	\$7,051	\$ -0-	\$ -0-	\$-0-	\$ -0-	\$7,051
Jiang He, Secretary	2011	\$4,500	\$ -0-	\$ -0-	\$-0-	\$ -0-	\$4,500
	2010	\$4,500	\$ -0-	\$ -0-	\$-0-	\$ -0-	\$4,500

(1) Reflects the grant date fair value of the awards calculated in accordance with FASB ASC Topic 718 – Stock Compensation.

(2) Mr. Dong was appointed to the position of Chief Financial Officer effective December 14, 2010. In accordance with the appointment, Mr. Dong received, on December 16, 2010, an option to purchase 200,000 shares of the Company's common stock under our 2003 Omnibus Plan. The option has a six (6) year term and vests 60,000 shares on the first anniversary of the date of grant and 70,000 shares on each of the second and third anniversaries of the date of grant, conditioned upon continued employment on such date. The exercise price of the option grant is \$2.12, the closing price on the date of the grant. The fair value of the option award is \$259,251, of which \$76,032 was recorded as compensation expenses for fiscal year ended October 31, 2011 and \$0 was recorded for fiscal year ended October 31, 2010.

(3) Ms. Lu was appointed to the position of interim Chief Financial Officer effective August 20, 2010 and replaced by Mr. Dong on December 14, 2010.

#### *Employment Agreements with Executive Officers*

On December 14, 2010, we entered into the CFO Appointment Agreement with Mr. Weiqiu Dong, who became our chief financial officer on that date. The agreement provides that Mr. Dong will receive an annual base salary of RMB 600,000 per year. In accordance with the appointment, Mr. Dong received, on December 16, 2010, an option to purchase 200,000 shares of the Company's common stock under our 2003 Omnibus Plan. The option has a six (6) year term and vests 60,000 shares on the first anniversary of the date of grant and 70,000 shares on each of the second and third anniversaries of the date of grant, conditioned upon continued employment on such date. The exercise price of the option grant is \$2.12, the closing price on the date of the grant. Fair market value of the option granted was \$259,251.

We have no other employment agreements with our executive officers. Our chairman, chief executive officer and president, Mr. Li receives \$31,250 in annual salary and is reimbursed for out of pocket expenses. Our secretary, Mr. He receives \$4,500 in annual salary and is reimbursed for out of pocket expenses.

#### *Benefit Plans*

We do not have any profit sharing plan or similar plans for the benefit of our officers, directors or employees. However, we may establish such plans in the future. Certain employees of our subsidiary, including Mr. Shaoming Li, our Chairman, Chief Executive Officer, and President, receive pension and healthcare benefits through plans offered by such subsidiary, as required by local Chinese laws.

#### *2007 Non-Qualified Company Stock Grant and Option Plan and 2003 Omnibus Securities Plan*

On March 19, 2007, our board of directors approved the 2007 Non-Qualified Company Stock Grant and Option Plan (the "2007 Plan"). The 2007 Plan is intended to serve as an incentive and to encourage stock ownership by our directors, officers, and employees, and certain persons rendering service to us, so that such persons may acquire or increase their proprietary interest in our success, and to encourage them to remain in our service. Under the 2007 Plan, up to 200,000 shares of our common stock may be subject to options.

On February 28, 2003, our board of directors approved our 2003 Omnibus Securities Plan (the “2003 Plan”), which was approved by our shareholders on April 11, 2003. The 2003 Plan offers selected employees, directors, and consultants the opportunity to acquire our common stock, and serves to encourage such persons to remain employed by us and to attract new employees. The 2003 Plan allows for the award of stock and options, up to 25,000 (after giving effect to the 1-for-30 reverse stock split in 2006) shares of our common stock. On May 1, of each year, the number of shares in the 2003 Securities Plan is automatically adjusted to an amount equal to ten percent of our outstanding stock on April 30, of the immediately preceding year. As of April 30, 2011, the number of shares of common stock outstanding was 37,239,536 making 3,723,954 shares of common stock subject to the 2003 Plan.



**Outstanding Equity Awards at October 31, 2011**

The following table sets forth certain information concerning unexercised options, stock that has not vested, and equity incentive plan awards outstanding as of October 31, 2011 for the named executive officers below:

**Outstanding Equity Awards at Fiscal Year Ended**

**October 31, 2011**

Name	Option Awards					Stock Awards			Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$)	
	Number of Securities Underlying Unexercised Options That Have Not Vested	Number of Securities Underlying Exercised Options	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Options	Option Exercise Price (\$)	Option Expiration Date	Number of Shares or Units That Have Not Vested	Market Value of Shares or Units That Have Not Vested (\$)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$)
Weiwei Dong(1)	0	200,000	0	\$ 2.12	12/16/2016	-	-	-	-	-

(1) 60,000 options vest on December 14, 2011, 70,000 options vest on December 14, 2012, and 70,000 options vest on December 14, 2013.

**Compensation of Directors**

The following table sets forth compensation paid to our non-executive directors for the fiscal year ended October 31, 2011.

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Name	Fees Paid in Cash (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity Incentive Plan Compensation (\$)	Nonqualified Deferred Compensation Earnings (\$)	All Other Compensation (\$)	Total (\$)
(a)	(b) <sup>(1)</sup>	(c) <sup>(2)</sup>	(d) <sup>(2)</sup>	(e)	(f)	(g)	
Zack Zibing Pan	1,250	-0-	34,042	<sup>(3)</sup> -0-	-0-	-0-	35,292
Bingchun Wu	5,527	-0-	-0-	-0-	-0-	-0-	5,527
Changxiong Sun	5,527	-0-	-0-	-0-	-0-	-0-	5,527
Xiaoheng Shao	36,000	-0-	-0-	<sup>(4)</sup> -0-	-0-	-0-	36,000

---

(1) The dollar value reflected is based on the average exchange rate for fiscal year 2011 with 1US Dollar equals to 6.52225RMB.

(2) Reflects the grant date fair value of the awards calculated in accordance with FASB ASC Topic 718 – Stock Compensation.

(3) We entered into an independent director agreement with Mr. Pan dated October 15, 2011, pursuant to which, as consideration for Mr. Pan's board services, we agreed to: (i) pay Mr. Pan a fee of \$2,500 per month, (ii) grant Mr. Pan an option to purchase 50,000 shares of common stock under the 2003 Plan, at an exercise price of \$0.80 per share, which is equal to the closing price of the Company's common stock on October 15, 2011, subject to vesting on a quarterly basis (4,166 shares of option to vest on the first 11 quarter anniversaries of the grant and 4,174 shares of option to vest on the 12th quarter anniversary of the grant with the initial 4,166 shares of option vesting to commence on January 15, 2012). The fair value of the option award is \$34,042, of which \$2,837 was recorded as compensation expenses for fiscal year ended October 31, 2011.

(4) We entered into an independent director agreement with Mr. Shao dated April 13, 2010, pursuant to which we granted Mr. Shao an option to purchase a total amount of 70,000 shares of our common stock under the 2003 Plan at a purchase price of \$2.57 per share. Mr. Shao serviced as a director ended on October 15, 2011 and was vested options to purchase an aggregate 34,998 shares of our common stock. The fair value of the option award is \$171,397, of which \$57,131 and \$31,462, respectively, were recorded as compensation expenses for fiscal years ended October 31, 2011 and 2010.

#### *Independent Director Agreements*

We currently have agreements with our independent directors.

On October 15, 2011, we entered into an independent director agreement with Mr. Pan, who became our director on October 15, 2011. The agreement provides that Mr. Pan, the Chair of our Audit Committee, will receive (i) a fee of \$2,500 per month, (ii) options to purchase 50,000 shares of common stock under the 2003 Plan, at an exercise price of \$0.80 per share, which is equal to the closing price of the Company's common stock on October 15, 2011, subject to vesting on a quarterly basis (4,166 shares of option to vest on the first 11 quarter anniversaries of the grant and 4,174 shares of option to vest on the 12th quarter anniversary of the grant with the initial 4,166 shares of option vesting to commence on January 15, 2012), and with all vesting conditional upon continued service as a director of the Company as of each such anniversary; and (iii) a reimbursement of out-of pocket expenses incidental to his services on the Board. The agreement expires on the earlier of (i) the date Mr. Pan ceases to be a member of the board, or (ii) the date of termination of the Agreement.

On April 19, 2010, we entered into an independent director agreement with Mr. Wu, who became a director on April 20, 2010. The agreement provides that Mr. Wu will receive a compensation of approximately RMB 3,000 per month for board meeting attendance as well as expense reimbursement. The Agreement expires on the earlier of (i) the date Mr. Wu ceases to be a member of the board, or (ii) the date of termination of the Agreement.

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

On April 19, 2010, we entered into an independent director agreement with Mr. Sun, who became a director on April 20, 2010. The agreement provides that Mr. Sun will receive a compensation of approximately RMB 3,000 per month for board meeting attendance as well as expense reimbursement. The Agreement expires on the earlier of (i) the date Mr. Sun ceases to be a member of the board, or (ii) the date of termination of the Agreement.

On April 13, 2010, we entered into an independent director agreement with Mr. Shao, who became a director on April 15, 2010. The agreement provides that Mr. Shao, the Chair of our Audit Committee, will receive a compensation of approximately \$3,000 per month for board meeting attendance as well as expense reimbursement. Additionally, Mr. Shao was granted an option to purchase up to 70,000 shares of our common stock under the 2003 Plan, at an exercise price of \$2.57 per share. The option will vest on a quarterly basis such that Mr. Shao will be entitled to purchase 5,833 shares of our common stock on the first 11 quarter anniversaries of the grant date (April 15, 2010) and 5,837 shares of our common stock on the twelfth quarter anniversary of the grant date. The option has a term of 3 years, starting from the date of grant. The agreement expires on the earlier of (i) the date Mr. Shao ceases to be a member of the board, or (ii) the date of termination of the Agreement. Mr. Shao ceased to be a director on October 15, 2011 and received 34,998 options for his past service with our company. The remaining 35,002 option shares have been cancelled.

There is currently no agreement with Mr. Li or Mr. Pi for compensation. Mr. Li and Mr. Pi are entitled to reimbursement for travel expenses. We do not pay additional amounts for committee participation or special assignments of the board of directors.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The following table sets forth, as of December 31, 2011, information concerning the beneficial ownership of shares of our common stock held by our directors, our named executive officers, our directors and executive officers as a group, and each person known by us to be a beneficial owner of 5% or more of our outstanding common stock.

Beneficial ownership is determined according to the rules of the SEC. Beneficial ownership means that a person has or shares voting or investment power of a security and includes any securities that person has the right to acquire within 60 days after the measurement date, such as those acquirable pursuant to options, warrants or convertible notes. Except as otherwise indicated, we believe that each of the beneficial owners of our common stock listed below, based on information each of them has given to us, has sole investment and voting power with respect to such beneficial owner's shares, except where community property or similar laws may apply. For purposes of the column for shares underlying convertible securities, in accordance with rules of the SEC, shares of our common stock underlying securities that a person has the right to acquire within 60 days of December 31, 2011 are deemed to be beneficially owned by such person for the purpose of computing the percentage ownership of that person, but we do not treat them as outstanding for the purpose of computing the ownership percentage of any other person.

Name and Address of Beneficial Owner	Common Stock Beneficially Owned				Percent <sup>(2)</sup>
	Total Outstanding	Underlying Convertible Securities <sup>(1)</sup>	Total		
<b>Directors and Named Executive Officers<sup>(3)</sup></b>					
Shaoming Li	17,850,000 <sup>(4)</sup>	0	17,850,000	47.9	%
Weiqiu Dong	21,800	60,000 <sup>(5)</sup>	81,800	*	
Zack Pan	0	4,166 <sup>(6)</sup>	4,166	*	
Xiaoheng Shao <sup>(7)</sup>	0	34,998 <sup>(7)</sup>	34,998	*	
Bingchun Wu	0	0	0	*	
Changxiong Sun	0	0	0	*	
Dianjun Pi	4,278,000 <sup>(8)</sup>	0	4,278,000	11.5	%
Jiang He	0	0	0	*	
Directors and executive officers as group (8 persons)	22,149,800 <sup>(9)</sup>	99,164	22,249,964	59.6	%
<b>5% Beneficial Owners</b>					
Tuya Wulan – New BVI Co <sup>(10)</sup> P.O. Box 957, Offshore Incorporation Center, Road Town, Tortola, British Virgin Islands	2,670,000	0	2,670,000	7.2	%
Cheung Yunman – Total Prosperity Company Limited <sup>(11)</sup> P.O. Box 957, Offshore Incorporation Center, Road Town, Tortola, British Virgin Islands	3,159,450	0	3,159,450	8.5	%

---

\*Individual owns less than 1% of our securities.

61

- (1) Includes shares of our common stock issuable upon exercise of options or upon conversion of warrants or convertible notes within 60 days.
- (2) Based on 37,239,536 shares of our common stock outstanding as of December 31, 2011.
- (3) The address for this beneficial owner is No. 281, Taiping Road, Taiping District, Harbin, Heilongjiang Province, China 150050.
- (4) Includes 17,850,000 shares of common stock owned by Celebrate Fortune Company Limited, an entity controlled by Mr. Shaoming Li.  
Includes options to purchase 60,000 shares of common stock as of December 31, 2011, with an exercise price of \$2.12 per share, in connection with option granted on December 14, 2010 to purchase 200,000 shares of our common stock. The option vest on an annual basis such that Mr. Dong is entitled to purchase 60,000 shares of our common stock on the first anniversary of the grant date and 70,000 shares of our common stock on the second and third anniversary of the grant date.
- (5) Includes options to purchase 4,166 shares of common stock as of December 31, 2011, with an exercise price of \$0.80 per share, in connection with option granted on October 15, 2011 to purchase 50,000 shares of our common stock. The option vest on a quarterly basis such that Mr. Pan is entitled to purchase 4,166 shares of our common stock on the first 11 quarter anniversaries of the grant date and 4,174 shares of our common stock on the twelfth quarter anniversary of the grant date.
- (6) Mr. Shao cease to be our director on October 15, 2011. Includes options to purchase 34,998 shares of our common stock.
- (7) Includes 4,278,000 shares of Common Stock owned by China Wealth Source Company Ltd, an entity controlled by Mr. Dianjun Pi.  
Includes 17,850,000 shares of Common Stock owned by Celebrate Fortune Company Limited, an entity controlled by Mr. Shaoming Li, and 4,278,000 shares of Common Stock owned by China Wealth Source Company Ltd, an entity controlled by Mr. Dianjun Pi.
- (8) Includes 2,670,000 shares of Common Stock owned by New BVI Co., an entity controlled by Mr. Tuya Wulan.
- (9) Includes 3,159,450 shares of Common Stock owned by Total Prosperity Company Limited, an entity controlled by Mr. Cheung Yunman.
- (10)
- (11)

### Securities Authorized for Issuance under Equity Compensation Plans

The following table provides aggregate information as of October 31, 2011 with respect to all compensation plans (including individual compensation arrangements) under which equity securities are authorized for issuance.

Plan Category	A	B	C
	Number of securities to be issued upon exercise of outstanding options, and warrants	Weighted-average exercise price of outstanding options, and warrants	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column A)
Equity compensation plans approved by security holders	284,998	\$ 1.96	3,438,956
	0	\$ 0.00	200,000



Equity compensation plans not approved by  
security holders(1)

Total	284,998	\$ 1.96	3,638,956
-------	---------	---------	-----------

(1) On March 19, 2007, our board of directors approved the 2007 Non-Qualified Company Stock Grant and Option Plan (the “2007 Plan”). The 2007 Plan was not approved by our shareholders. The 2007 Plan is intended to serve as an incentive and to encourage stock ownership by our directors, officers, and employees, and certain persons rendering service to us, so that such persons may acquire or increase their proprietary interest in our success, and to encourage them to remain in our service. Under the 2007 Plan, up to 200,000 shares of our common stock may be subject to options.

### **Item 13. Certain Relationships and Related Transactions, and Director Independence**

#### **Transactions with Related Persons:**

Mr. Shaoming Li, our chairman, chief executive officer and president, is also chairman and a 50% shareholder of Renhuang Stock. On October 12, 2009, we entered into a purchase agreement with Renhuang Stock to acquire the land use right, property and a plant located in Ah City for a total consideration of \$25,096,070. Pursuant to the purchase agreement, payments of \$23,527,566 have been made to Renhuang Stock before October 31, 2011, with a final payment of \$1,568,504 due by December 31, 2011, at which time title for the assets will be transferred. As we have not received all the required transfer documents from related local government authorities, the Company has to postpone the title transfer until all the transfer documents been received. The final payment will be made to Renhuang Stock at the time of title transfer. According to the agreement, we were exempted from lease payments for the underlying assets starting from May 1, 2010.

We lease property and a plant from Renhuang Stock. Under the lease terms, we no longer pay rent to Renhuang Stock for the use of the property and plant. However, the rental expenses related to this lease, incurred and expensed to consolidated statements of operations and comprehensive income during the year ended October 31, 2011 and 2010 amounted to \$766,607 and \$367,224, respectively, which were forgiven rental expenses and recognized to account for the rental exemption pursuant to the purchase agreement, and the deposits for the property were reduced accordingly.

On September 1, 2009, we entered into a Purchase Agreement with Renhuang Stock, to acquire two production patents, for a total consideration of \$2,509,607. Pursuant to the Purchase Agreement, a payment of \$1,568,504 was made to Renhuang Stock, in October 2009 and recorded as deposits on the consolidated balance sheet. Pursuant to the Purchase Agreement, final payment of \$941,103 is due by December 31, 2010, at which time title for the assets will be transferred. In August, 2010, final payment was made to Renhuang Stock and the tile of the patent was transferred at the same month.

#### **Review, Approval or Ratification of Transactions with Related Persons**

Our Audit Committee reviews and approves or ratifies any related person transaction that is required to be disclosed as such transactions required the approval of our Audit Committee. We did not have any related party transactions during fiscal years ended October 31, 2011 and 2010.

### **Item 14. Principal Accountant Fees and Services**

On January 13, 2010, we engaged Windes & McClaughry Accountancy Corporation (“W&M”) as our independent registered public accounting firm.

**Audit Fees**

During the year ended October 31, 2011 and 2010, the fees for W&M were approximately \$194,000 and \$195,000, respectively. The fees were for professional services for the audit of our Form 10-K financial statements and review of our quarterly Form 10-Q financial statements.

**Audit-Related Fees**

During the years ended October 31, 2011 and 2010, there were no fees relating to the performance of any other audit or review of our financial statements by W&M.

**Tax Fees**

During the years ended October 31, 2011 and 2010, there were no fees relating to professional tax services by W&M.

**All Other Fees**

During the years ended October 31, 2011 and 2010, there were no other fees relating to services provided by W&M.

The above-mentioned fees are set forth as follows in tabular form:

	2011	2010
Total Audit Fees	\$194,000	\$195,000
Total Audit Related Fees	\$-0-	\$-0-
Total Tax Fees	\$-0-	\$-0-
Total of All Other Fees	-0-	-0-

All services and fees described above for the years ended October 31, 2011 and 2010 were approved by either the entire board of directors or the Audit Committee. The Audit Committee's pre-approval policies and procedures were detailed as to the particular service and the audit committee was informed of each service and such policies and procedures did not include the delegation of the audit committee's responsibilities.

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

**Financial Statements**

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

*(a) Financial Statements:*

	Page
Report of Windes & McClaughry Accountancy Corporation	F-2
Consolidated Balance Sheets at October 31, 2011 and 2010	F-3
Consolidated Statements of Operations and Comprehensive Income for the Years Ended October 31, 2011 and 2010	F-4
Consolidated Statements of Changes in Shareholders' Equity for the Years Ended October 31, 2011 and 2010	F-5
Consolidated Statements of Cash Flows for the Years Ended October 31, 2011 and 2010	F-6
Notes to Consolidated Financial Statements	F-7

## Exhibits

The following exhibits are filed as a part of this Annual Report.

### Exhibit

No.	Description
3.1	Restated Articles of Incorporation <sup>(1)</sup>
3.2	Amended and Restated Bylaws <sup>(2)</sup>
3.3	Certificate of Amendment to Articles of Incorporation <sup>(3)</sup>
3.4	Certificate of Amendment to Articles of Incorporation reflecting change of name to China Botanic Pharmaceutical Inc. <sup>(4)</sup>
10.1	2007 Non-Qualified Company Stock Grant and Option Plan <sup>(5)</sup>
10.2	2003 Omnibus Securities Plan <sup>(6)</sup> Loan Conversion Agreement among the Company, Allied Merit International Inc. and Griffin Ventures Ltd. dated May 15, 2009 <sup>(7)</sup>
10.3	Employment Agreements with Weiqiu Dong <sup>(4)</sup>
10.4	English translation of Purchase Agreement for Patents dated September 1, 2009 <sup>(8)</sup>
10.5	English translation of Purchase Agreement for Ah City Natural and Biopharmaceutical plant dated October 12, 2009 <sup>(8)</sup>
10.6	English translation of Purchase Agreement with Hongxiangmingyuan of Heilongjiang Yongtai Company dated April 10, 2010 <sup>(9)</sup>
10.7	Independent Director Agreement with Mr. Xiaoheng (Sean) Shao, dated April 13, 2010 <sup>(9)</sup>
10.8	Independent Director Agreement with Mr. Bingchun Wu, dated April 19, 2010 <sup>(9)</sup>
10.9	Independent Director Agreement with Mr. Changxiong Sun, dated April 19, 2010 <sup>(9)</sup>
10.10	Independent Director Agreement with Mr. Zack Plan, dated October 15, 2011*
10.11	English translation of the Exclusive Licensing Agreement for Harbin Renhuang Pharmaceutical Co., Ltd. to Use Forest Resources under Yichun Red Star Forestry Bureau *
21.1	Subsidiaries of the registrant <sup>(3)</sup>
23.2	Consent Of Windes & McClaughry Accountancy Corporation*
31.1	Certification of Principal Executive Officer pursuant to Rules 13a-14 and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
31.2	Certification of Principal Financial Officer pursuant to Rules 13a-14 and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*
101.INS	XBRL Instance Document (10)
101.SCH	XBRL Taxonomy Extension Schema (10)
101.CAL	XBRL Taxonomy Extension Calculation Linkbase (10)
101.DEF	XBRL Taxonomy Extension Definition Linkbase (10)
101.LAB	XBRL Taxonomy Extension Label Linkbase (10)
101.FRE	XBRL Taxonomy Extension Presentation Linkbase (10)

\* Filed herewith.

- (1) Incorporated by reference from Form 8-K filed with the SEC on April 22, 2003.
- (2) Incorporated by reference from Form 8-K filed with the SEC on January 10, 2012.
- (3) Incorporated by reference from Form 10-K filed with the SEC on February 13, 2007.
- (4) Incorporated by reference from Form 10-K filed with the SEC on January 24, 2011.
- (5) Incorporated by reference from Form 8-K filed with the SEC on May 2, 2007.
- (6) Incorporated by reference from Form 8-K filed with the SEC on April 22, 2003.
- (7) Incorporated by reference from Form 10-Q filed with the SEC on September 21, 2009.
- (8) Incorporated by reference from Form 10-K filed with the SEC on January 29, 2010.
- (9) Incorporated by reference from Form 10-Q filed with the SEC on June 7, 2010.

- (10) XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Report to be signed on our behalf by the undersigned, thereunto duly authorized.

Date: January 30, 2012 CHINA BOTANIC PHARMACEUTICAL INC.

By: /s/ Shaoming Li  
Shaoming Li, Chief Executive Officer and President  
(Principal Executive Officer)

Date: January 30, 2012 By: /s/ Weiqiu Dong  
Weiqiu Dong, Chief Financial Officer  
(Principal Accounting and Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following person on behalf of the registrant and in the capacity and on the dates indicated.

Date: January 30, 2012 /s/ Shaoming Li  
Shaoming Li,  
Chief Executive Officer, President, Chairman of the Board

Date: January 30, 2012 /s/ Zack Zibing Pan  
Zack Zibing Pan, Director

Date: January 30, 2012 /s/ Changxiong Sun  
Changxiong Sun, Director

Date: January 30, 2012 /s/ Bingchun Wu  
Bingchun Wu, Director

Date: January 30, 2012 /s/ Dianjun Pi  
Dianjun Pi, Director

Date: January 30, 2012 /s/ Weiqiu Dong  
Weiqiu Dong, Chief Financial Officer



**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Report of Independent Registered Public Accounting Firm	F-2
Consolidated Balance Sheets As of October 31, 2011 and 2010	F-3
Consolidated Statements of Operations and Comprehensive Income for Years Ended October 31, 2011 and 2010	F-4
Consolidated Statements of Changes in Shareholders' Equity for Years Ended October 31, 2011 and 2010	F-5
Consolidated Statements of Cash Flows for Years Ended October 31, 2011 and 2010	F-6
Notes to Consolidated Financial Statements for Years Ended October 31, 2011 and 2010	F-7

F-1

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and

Stockholders of China Botanic Pharmaceutical Inc.

We have audited the accompanying consolidated balance sheets of China Botanic Pharmaceutical Inc. as of October 31, 2011 and 2010, and the related consolidated statements of operations and comprehensive income, shareholders' equity, and cash flows for each of the years in the two-year period ended October 31, 2011. China Botanic Pharmaceutical Inc.'s management is responsible for these consolidated financial statements. 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 financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of China Botanic Pharmaceutical Inc. as of October 31, 2011 and 2010, and the results of their operations and their cash flows for the years in the two-year period ended October 31, 2011 in conformity with accounting principles generally accepted in the United States of America.

/s/ Windes & McClaughry Accountancy Corporation

Windes & McClaughry Accountancy Corporation

Long Beach, California

January 30, 2012

F-2

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

	Note	October 31, 2011	October 31, 2010
<b>ASSETS</b>			
Current assets:			
Cash		\$15,283,583	\$27,826,142
Trade receivables, net	5	21,548,325	19,814,438
Due from related parties	11	—	28,877
Inventory, net	7	7,416,720	2,645,616
Other receivables, net	6	6,823,410	200,994
Total current assets		51,072,038	50,516,067
Property and equipment, net	8	1,778,984	2,069,460
Intangible Assets	9	17,146,700	1,953,617
Construction in progress	10	1,937,103	—
Deposits for properties	11,12	37,822,113	18,605,935
Deferred tax assets	13	139,226	—
Total assets		\$109,896,164	\$73,145,079
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
Liabilities			
Accounts payable		\$2,098,256	\$333,555
Tax payable		5,976,417	1,064,066
Accrued employee benefits	16	2,131,565	1,645,192
Warrant Liabilities	19	23,443	342,770
Total liabilities		10,229,681	3,385,583
Shareholders' equity			
Preferred stock (no par value, 1,000,000 shares authorized; none issued and outstanding as of October 31,2011 and October 31, 2010,respectively)	18		
Common stock (\$0.001 par value, 100,000,000 shares, authorized; 37,239,536 issued and outstanding as of October 31,2011 and October 31, 2010, respectively)	18	37,240	37,240
Additional paid-in capital		7,763,987	7,627,987
Common stock warrants	19	496,732	496,732
Reserves	20	3,372,697	3,372,697
Accumulated other comprehensive income		8,620,695	4,768,793
Retained earnings		79,375,132	53,456,047
Total shareholders' equity		99,666,483	69,759,496

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Total liabilities and shareholders' equity	\$ 109,896,164	\$ 73,145,079
--	----------------	---------------

The accompanying notes are an integral part of these consolidated financial statements.

F-3

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME**

		For the year ended October 31,	
	Note	2011	2010
Sales, net		\$72,713,748	\$55,183,941
Cost of goods sold		29,531,087	25,765,835
Gross profit		43,182,661	29,418,106
Operating and administrative expenses:			
Sales and distribution		6,024,230	4,966,062
General and administrative		4,046,197	3,614,809
Research and development		3,592,555	3,042,815
Total operating expenses		13,662,982	11,623,686
Income from operations		29,519,679	17,794,420
Other income:			
Interest income		126,943	74,522
Income before income tax expenses		29,646,622	17,868,942
Income tax expenses	14	3,727,537	—
Net income		\$25,919,085	\$17,868,942
Other comprehensive income:			
Cumulative currency translation adjustments		3,851,902	1,401,134
Total comprehensive income		\$29,770,987	\$19,270,076
Earnings per common stock- Basic	15	\$0.70	\$0.48
Earnings per common stock - Diluted		\$0.69	\$0.47
Weighted average common stock outstanding	15		
Basic		37,239,536	37,239,536
Diluted		37,678,525	37,778,028

The accompanying notes are an integral part of these consolidated financial statements.

F-4

## CHINA BOTANIC PHARMACEUTICALS, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Common stock (\$0.001 par value)		Additional	Common		Accumulated	Retained	Total
	Number of	Par	Paid-in	Stock	Reserves	Other	Earnings	Shareholders'
	Shares	Value	Capital	Warrants	US\$	Income	US\$	Equity
		US\$	US\$	US\$	US\$	US\$	US\$	US\$
Balance as of								
October 31, 2009	37,239,536	37,240	7,596,525	496,732	3,372,697	3,367,659	35,587,105	50,457,958
Option Granted	—	—	31,462	—	—	—	—	31,462
Net income	—	—	—	—	—	—	17,868,942	17,868,942
Currency translation adjustments	—	—	—	—	—	1,401,134	—	1,401,134
Balance as of								
October 31, 2010	37,239,536	37,240	7,627,987	496,732	3,372,697	4,768,793	53,456,047	69,759,496
Net income	—	—	—	—	—	—	25,919,085	25,919,085
Option Granted	—	—	136,000	—	—	—	—	136,000
Currency translation adjustments	—	—	—	—	—	3,851,902	—	3,851,902
Balance as of								
October 31, 2011	37,239,536	37,240	7,763,987	496,732	3,372,697	8,620,695	79,375,132	99,666,483

The accompanying notes are an integral part of these consolidated financial statements.



**CHINA BOTANIC PHARMACEUTICALS, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

	For the year ended October 31,	
	2011	2010
	US\$	US\$
Cash flows from operating activities:		
Net income	\$ 25,919,085	\$ 17,868,942
Adjustments to reconcile net income to operating activities:		
Depreciation	383,846	363,567
Amortization	569,643	435,653
Warrants issued for service	(319,327 )	342,770
Share Compensation	136,000	31,462
Forgiven Rent	1,028,781	367,224
Deferred tax assets	(136,093 )	—
Changes in assets and liabilities:		
(Increase)Decrease in trade receivables	(794,722 )	3,814,889
(Increase)Decrease in due from related parties	29,539	(28,300 )
(Increase) Decrease in inventory, net	(4,543,566 )	423,480
Decrease in prepayments	—	89,397
(Increase) in other receivables, net	(6,464,282 )	(94,232 )
Decrease in accounts payable	(5,017 )	(44,546 )
Increase(Decrease) in tax payable	4,753,483	(145,371 )
Increase in accrued employee benefits	400,691	442,040
(Decrease) increase in other payable	181,646	(31,413 )
Net cash provided by operating activities	21,139,707	23,835,562
Cash flows from investing activities:		
Deposits for land use right and properties	(21,464,985 )	(3,944,749 )
Deposits for patents	(11,299,782 )	(717,926 )
Construction in progress	(1,893,518 )	—
Purchase of property and equipment	(5,891 )	(36,473 )
Net cash used in investing activities	(34,664,176 )	(4,699,148 )
Cash flows from financing activities:		
Net cash provided by financing activities	—	—
Effect of exchange rate changes on cash	981,910	578,214
Net increase (decrease) in cash	(12,542,559 )	19,714,628
Cash, beginning of year	27,826,142	8,111,514
Cash, end of year	\$ 15,283,583	\$ 27,826,142

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Supplemental disclosure of cash flow information:

Cash paid during the year for income taxes	\$—	\$—
Interest paid during the year	\$—	\$—

The accompanying notes are an integral part of these consolidated financial statements.

F-6

## CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES

### NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

#### 1. ORGANIZATION AND NATURE OF OPERATION

The accompanying consolidated financial statements include the financial statements of China Botanic Pharmaceutical Inc. (“CBP”) and its subsidiaries. CBP and its subsidiaries are collectively referred to as the “Company.”

CBP was incorporated in the State of Nevada on August 18, 1988, originally under the corporate name of Solutions, Incorporated. It was inactive until August 16, 1996, when it changed its corporate name to Suarro Communications, Inc, and engaged in the business of providing internet based business services. This line of business was discontinued in 2006, and CBP became a non-operating public company. CBP underwent a number of corporate name changes as follows:

June 1997	ComTech Consolidation Group, Inc
February 1999	E-Net Corporation
May 1999	E-Net Financial Corporation
January 2000	E-Net.Com Corporation
February 2000	E-Net Financial.Com Corporation
January 2002	Anza Capital, Inc (“Anza”)
June 2006	Renhuang Pharmaceuticals, Inc.
October 2010	China Botanic Pharmaceutical Inc.

Effective August 28, 2006, CBP completed the acquisition of 100% ownership of Harbin Renhuang Pharmaceutical Company Limited, a company incorporated in the British Virgin Islands. As a result, Harbin Renhuang Pharmaceutical Company Limited became a wholly owned subsidiary of CBP

Harbin Renhuang Pharmaceutical Company Limited owns 100% of the registered capital of Harbin Renhuang Pharmaceutical Co. Ltd (“CBP China”).

The core activities of subsidiaries included in the consolidated financial statements are as follow:

- Harbin Renhuang Pharmaceutical Company Limited – Investment holding.
- CBP China – Development, manufacturing and distribution of pharmaceutical products.

CBP China's principal country of operations is the People's Republic of China (the "PRC") and maintains their accounting records in Renminbi ("RMB"). Substantially all of the Company's assets and operation are located in the PRC.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### a. **Basis of presentation of financial statements**

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP") and are expressed in terms of US dollars.

In June 2009, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard ("SFAS") No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles, a replacement of FASB Statement No. 162*. This statement modifies the Generally Accepted Accounting Principles ("GAAP") hierarchy by establishing only two levels of GAAP, authoritative and nonauthoritative accounting literature. Effective July 2009, the FASB Accounting Standards Codification ("ASC"), also known collectively as the "Codification," is considered the single source of authoritative U.S. accounting and reporting standards, except for additional authoritative rules and interpretive releases issued by the SEC. Nonauthoritative guidance and literature would include, among other things, FASB Concepts Statements, American Institute of Certified Public Accountants Issue Papers and Technical Practice Aids and accounting textbooks. The Codification was developed to organize GAAP pronouncements by topic so that users can more easily access authoritative accounting guidance. It is organized by topic, subtopic, section, and paragraph, each of which is identified by a numerical designation. This statement applies beginning in third quarter 2009. All accounting references have been updated, and therefore SFAS references have been replaced with ASC references.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

The Company operates in one operating segment in accordance with accounting guidance FASB ASC Topic 280, “*Segment Reporting*.” Our CEO has been identified as the chief operating decision maker as defined by FASB ASC Topic 280.

**b. Principles of consolidation**

The consolidated financial statements include the financial statements of CBP and its subsidiaries.

All inter-company transactions and balances have been eliminated in consolidation.

Effective beginning third quarter 2009, the FASB Topic 810, “*Consolidation Topic*,” revised the accounting treatment for noncontrolling minority interests of partially-owned subsidiaries. Noncontrolling minority interests represent the portion of earnings that is not within the parent company’s control. These amounts are now required to be reported as equity instead of as a liability on the balance sheet. In addition this statement requires net income from noncontrolling minority interest to be shown separately on the consolidated statements of operations and comprehensive income. As the Company has no noncontrolling interest at October 31, 2011, this change did not have an impact on the Company’s consolidated financial statements.

**c. Use of estimates**

The preparation of these consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affected the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of net sales and expenses during the reported periods.

Significant estimates and assumptions by management include, among others, uncollectible accounts receivable, slow moving, obsolete and/or damaged inventory, property and equipment, reserve for employee benefit obligations, stock warrant valuation, and other uncertainties. Actual results may differ from these estimates. The current economic environment has increased the degree of uncertainty inherent in these estimates and assumptions.

**d. Foreign currency translation**

The Company's principal country of operations is in PRC. The financial position and results of operations of the subsidiaries are determined using the local currency ("Renminbi" or "RMB") as the functional currency.

Translation of amounts from RMB into US dollars for reporting purposes is performed by translating the results of operations denominated in foreign currency at the weighted average rate of exchange during the reporting period. Assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the market rate of exchange ruling at that date. The registered equity capital denominated in the functional currency is translated at the historical rate of exchange at the time of capital contribution. All translation adjustments resulting from the translation of the financial statements into the reporting currency (US dollars) are reported as a component of accumulated other comprehensive income in shareholders' equity.

As of October 31, 2011 and 2010, the exchange rate was RMB 6.38 and RMB 6.67, respectively. Translation adjustments totaled \$3,851,902 and \$1,401,134 for the year ended October 31, 2011 and 2010, respectively.

**e. Cash**

There are no restriction to cash at October 31, 2011 and 2010. Substantially all of the Company's cash is held in bank accounts in the PRC and is not protected by the Federal Deposit Insurance Corporation ("FDIC") insurance or any other similar insurance. Given the current economic environment and risks in the banking industry, there is a risk that deposits may not be readily available.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**f. Trade receivables, net**

Trade receivables are recorded at the invoiced amount and do not bear interest. Trade receivable payment terms vary and amounts due from customers are stated in the financial statements net of an allowance for doubtful accounts and sales rebates. The Company maintains an allowance for doubtful accounts for estimated losses inherent in its trade receivables. Trade receivables outstanding longer than the payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time the trade receivable is past due, the Company's previous loss history, the counter party's current ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes off receivables when they are deemed uncollectible, and payments subsequently received on such trade receivables are credited to the allowance for doubtful accounts. There were no write offs for the years ended October 31, 2011 and 2010. The Company does not have any off-balance sheet credit exposure related to its customers.

**g. Inventory, net**

Inventory consists of raw materials, work-in-progress and finished goods and is valued at the lower of cost or market value. The value of inventory is determined using the weighted average cost method and includes any related production overhead costs incurred in bringing the inventory to their present location and condition. Overhead costs included in finished goods include, direct labor cost and other costs directly applicable to the manufacturing process.

The Company estimates an inventory allowance for excessive, slow moving and obsolete inventories as well as inventory whose carrying value is in excess of net realizable value. Inventory amounts are reported net of such allowances. There were no inventory write offs for the years ended October 31, 2011 and 2010.

**h. Property and equipment, net**

Property and equipment are recorded at cost. Expenditures for major additions and improvements are capitalized and minor replacements, maintenance, and repairs are charged to expense as incurred. When property and equipment are retired or otherwise disposed of, the cost and accumulated depreciation are removed from the accounts and any resulting gain or loss is included in the results of operations for the respective period.

Depreciation is provided over the estimated useful lives of the related assets using the straight-line method. The estimated useful lives for significant property, plant and equipment categories are as follows:

Machinery and equipment	10 years
Office equipment and furnishings	5-10 years
Motor vehicles	5-10 years

**i. Intangible assets, net**

Intangible assets consist of purchased patents. Intangible assets are carried at cost less accumulated amortization and any impairment. Intangible assets with a finite useful life are amortized using the straight-line method over valid periods varied from 10 to 30 years, which is the estimated economic life of the intangible assets.

**j. Accounting for the impairment of long-lived assets**

The Company's long-lived assets and other assets (consisting of property and equipment) are reviewed for impairment in accordance with the guidance of the FASB Topic ASC 360, "*Property, Plant, and Equipment*," FASB Topic ASC 360, "*Intangibles - Goodwill and Others*," and FASB ASC Topic 205 "*Presentation of Financial Statements*." The Company tests for impairment losses on long-lived assets used in operations whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. Recoverability of an asset to be held and used is measured by a comparison of the carrying amount of an asset to the future undiscounted cash flows expected to be generated by the asset. If such asset is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds its fair value. Impairment evaluations involve management's estimates on asset useful lives and future cash flows. Actual useful lives and cash flows could be different from those estimated by management which could have a material effect on our reporting results and financial positions. Fair value is determined through various valuation techniques including discounted cash flow models, quoted market values and third-party independent appraisals, as considered necessary. Through the years ended October 31, 2011 and 2010, the Company had not experienced impairment losses on its long-lived assets. However, there can be no assurances that demand for the Company's products or services will continue, which could result in an impairment of long-lived assets in the future.



**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**k. Fair value of financial instruments**

The Company applies the provisions of accounting guidance, FASB Topic ASC 825 that requires all entities to disclose the fair value of financial instruments, both assets and liabilities recognized and not recognized on the balance sheet, for which it is practicable to estimate fair value, and defines fair value of a financial instrument as the amount at which the instrument could be exchanged in a current transaction between willing parties. As of October 31, 2011 and 2010 the carrying value of cash, trade receivables, other receivables, accounts payable, approximated their fair value. All derivatives are recorded at fair value evaluated based on Black-Scholes option model.

**l. Fair value measurements**

Effective April 1, 2009, the FASB ASC Topic 825, "*Financial Instruments*," requires disclosures about fair value of financial instruments in quarterly reports as well as in annual reports.

The FASB ASC Topic 820, "*Fair Value Measurements and Disclosures*," clarifies the definition of fair value for financial reporting, establishes a framework for measuring fair value and requires additional disclosures about the use of fair value measurements.

Various inputs are considered when determining the fair value of the Company's financial instruments. The inputs or methodologies used for valuing securities are not necessarily an indication of the risk associated with investing in these securities. These inputs are summarized in the three broad levels listed below.

Level 1 – observable market inputs that are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2 – other significant observable inputs (including quoted prices for similar securities, interest rates, credit risk, etc.).

Level 3 – significant unobservable inputs (including the Company’s own assumptions in determining the fair value of financial instruments).

The Company’s adoption of FASB ASC Topic 825 did not have a material impact on the Company’s consolidated financial statements.

The carrying value of financial assets and liabilities recorded at fair value is measured on a recurring or nonrecurring basis. Financial assets and liabilities measured on a non-recurring basis are those that are adjusted to fair value when a significant event occurs. The Company had no financial assets or liabilities carried and measured on a nonrecurring basis during the reporting periods. Financial assets and liabilities measured on a recurring basis are those that are adjusted to fair value each time a financial statement is prepared.

The availability of inputs observable in the market varies from instrument to instrument and depends on a variety of factors including the type of instrument, whether the instrument is actively traded, and other characteristics particular to the transaction. For many financial instruments, pricing inputs are readily observable in the market, the valuation methodology used is widely accepted by market participants, and the valuation does not require significant management discretion. For other financial instruments, pricing inputs are less observable in the market and may require management judgment.

**m. Revenue recognition**

Revenue is recognized in accordance with Staff Accounting Bulletin No. 104, “*Revenue Recognition*,” which states that revenue should be recognized when the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) the service has been rendered; (3) the selling price is fixed or determinable; and (4) collection of the resulting receivable is reasonably assured.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

Interest income is recognized when earned, taking into account the average principal amounts outstanding and the interest rates applicable.

As of October 31, 2011, the Company has no sales or contracts that included multiple deliverables that would fall under the scope of FASB Topic ASC 605, “*Multiple Deliverable Revenue Arrangements – A Consensus of the FASB Emerging Issues Task Force.*”

The Company provided annual sales rebates to its distributors based upon sales volumes. Sales rebates are recorded as a current liability at the time of the sale based upon the Company’s estimates of whether each customer would be entitled to rebates for the period. At quarter end, the accrued rebate amount is adjusted to the actual amount earned and reclassified to trade receivables in accordance with legal right of offset. Sales rebates were deducted from sales in the accompanying consolidated statements of operations and comprehensive income.

As of October 31, 2011 and, 2010, the Company has accrued \$1,681,721 and \$2,141,055, respectively, for sales rebates, which offset the balance of account receivables. For the years ended October 31, 2011 and 2010, the Company has deducted sales rebates in the amount of \$6,894,477 and \$7,516,231, respectively, from sales. Sales rebates are calculated based on terms specified in contracts with individual distributors.

**n. Sales returns and allowances**

The Company does not allow return of products except for products that were damaged during shipment. The total amount of returned product is less than 0.05% of total sales. The cost of damaged products is netted against sales and cost of goods sold, respectively.

**o. Cost of goods sold**

Cost of goods sold primarily consists of direct and indirect manufacturing costs, including raw material, packaging material, production overhead costs, city construction tax and educational tax for the products sold.

**p. Sales and marketing**

Sales and marketing costs consist primarily of advertising and market promotion expenses, and other overhead expenses incurred by the Company's sales and marketing personnel. Advertising expenses are expensed as incurred and amounted to \$5,772,548 and \$4,803,286 during the years ended October 31, 2011 and 2010 respectively.

**q. Research and development**

Research and development ("R&D") consists primarily of cost of materials and overhead expenses r by research and development staff. Research and development costs are expensed as incurred. Research and development expenses amounted to \$3,592,555 and \$3,042,815 during the years ended October 31, 2011 and 2010 respectively.

**r. Employee benefit costs**

According to the PRC regulations on pension, a company contributes to a defined contribution retirement plan organized by municipal government in the province in which the CBP China was registered and all qualified employees are eligible to participate in the plan. Contributions to the plan are calculated at 22% of the employees' salaries above a fixed threshold amount.

**s. Share-based compensation**

For purposes of determining the variables used in the calculation of stock compensation expense under the provisions of FASB ASC Topic 505, "*Equity*" and FASB ASC Topic 718, "*Compensation — Stock Compensation*," we perform an analysis of current market data and historical Company data to calculate an estimate of implied volatility, the expected term of the option and the expected forfeiture rate. With the exception of the expected forfeiture rate, which is not an input, we use these estimates as variables in the Black-Scholes option pricing model. Depending upon the number of stock options granted, any fluctuations in these calculations could have a material effect on the results presented in our consolidated statement of income and other comprehensive income. In addition, any differences between estimated forfeitures and actual forfeitures could also have a material impact on our financial statements.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**t. Taxation**

Taxation on profits earned in the PRC has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the PRC in which the Company operates after taking into effect the benefits from any special tax credits or “tax holidays” allowed in the country of operations.

The Company accounts for income tax under the provisions of FASB ASC Topic 740, “*Income Taxes*,” which requires recognition of deferred tax assets and liabilities for the expected future tax consequences of the events that have been included in the financial statements or tax returns. Deferred income taxes are recognized for all significant temporary differences between tax and financial statements bases of assets and liabilities. Valuation allowances are established against net deferred tax assets when it is more likely than not that some portion or all of the deferred tax asset will not be realized.

The Company does not have any long-term deferred tax assets or liabilities in China that will exist once the tax holiday expires. The Company does not have any significant deferred tax asset or liabilities that relate to tax jurisdictions not covered by the tax holiday.

The Company does not accrue United States income tax on unremitted earnings from foreign operations, as it is the Company’s intention to invest these earnings in the foreign operations indefinitely.

Generally, years beginning after fiscal 2006, the Company is open to examination by PRC taxing authorities. In the United States, we are open to examination from 2006 onward.

*Enterprise income tax*

On March 16, 2007, the PRC National People’s Congress passed the PRC Enterprise Income Tax Law (“New EIT Law”) which became effective on January 1, 2008. Pursuant to the New EIT Law, a unified enterprise income tax rate of 25 percent and unified tax deduction standards will be applied consistently to both domestic-invested enterprises and

foreign-invested enterprises. However, the New EIT Law repealed most of the existing preferential tax rates and tax holidays. A five-year transition period is allowed for enterprises that obtained preferential tax treatment under the prior tax regime. Under the prior tax regime, foreign-invested enterprises were generally subject to a 30 percent federal tax rate plus a 3 percent local tax rate for a total tax rate of 33 percent.

CBP China secured preferential tax treatment in the jurisdiction where it conducts its manufacturing activity, where it was granted tax exemption of 10% from the government, for being a new and high-technology enterprise.

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 basis. Deferred tax assets, including tax loss and credit carry forwards, 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 of deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income tax expense represents the change during the period in the deferred tax assets and deferred tax liabilities. The components of the deferred tax assets and liabilities are individually classified as current and noncurrent based on their characteristics. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

A provision has not been made at October 31, 2011 for U.S. or additional foreign withholding taxes on approximately \$79,375,132 of undistributed earnings of foreign subsidiaries because it is the present intention of management to reinvest the undistributed earnings indefinitely in foreign operations. Generally, such earnings become subject to U.S. tax upon the remittance of dividends and under certain other circumstances. It is not practicable to estimate the amount of deferred tax liability on such undistributed earnings.

## CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES

### NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

The Company recognizes that virtually all tax positions in the PRC are not free of some degree of uncertainty due to tax law and policy changes by the State. However, the Company cannot reasonably quantify political risk factors and thus must depend on guidance issued by current State officials.

Based on all known facts and circumstances and current tax law, the Company believes that the total amount of unrecognized tax benefits as of October 31, 2011, is not material to its results of operations, financial condition or cash flows. The Company also believes that the total amount of unrecognized tax benefits as of October 31, 2011, if recognized, would not have a material effect on its effective tax rate. The Company further believes that there are no tax positions for which it is reasonably possible, based on current Chinese tax law and policy, that the unrecognized tax benefits will significantly increase or decrease over the next 12 months producing, individually or in the aggregate, a material effect on the Company's results of operations, financial condition or cash flows.

#### *Value added tax*

The Provisional Regulations of The People's Republic of China Concerning Value Added Tax promulgated by the State Council came into effect on January 1, 1994. Under these regulations and the Implementing Rules of the Provisional Regulations of the PRC Concerning Value Added Tax, value added tax is imposed on goods sold in or imported into the PRC and on processing, repair and replacement services provided within the PRC.

Value added tax payable in The People's Republic of China is charged on an aggregated basis at a rate of 13% or 17% (depending on the type of goods involved) on the full price collected for the goods sold or, in the case of taxable services provided, at a rate of 17% on the charges for the taxable services provided, but excluding, in respect of both goods and services, any amount paid in respect of value added tax included in the price or charges, and less any deductible value added tax already paid by the taxpayer on purchases of goods and services in the same financial year.

#### **u. Comprehensive Income**

Total comprehensive income is defined as all changes in shareholders' equity during a period, other than those resulting from investments by and distributions to shareholders (i.e., issuance of equity securities and dividends). Generally, for the Company, total comprehensive income equals net income plus or minus adjustments for currency

translation. Total comprehensive income represents the activity for a period net of related tax and was \$29,770,987 and \$19,270,076 for the years ended October 31, 2011 and 2010, respectively.

While total comprehensive income is the activity in a period and is largely driven by net earnings in that period, accumulated other comprehensive income or loss ("AOCI") represents the cumulative balance of other comprehensive income as of the balance sheet date. For the Company, AOCI is primarily the cumulative balance related to the currency adjustments and increased overall equity by \$3,851,902 and \$ 1,401,134 as of October 31, 2011 and 2010 respectively.

v. **Earnings per share**

Basic net earnings per common stock are computed by dividing net earnings applicable to common shareholders by the weighted-average number of common stock outstanding during the period. Diluted net earnings per common stock is determined using the weighted-average number of common stock outstanding during the period, adjusted for the dilutive effect of common stock equivalents, using the treasury stock method, consisting of shares that might be issued upon exercise of common stock warrants. In periods where losses are reported, the weighted-average number of common stock outstanding excludes common stock equivalents, because their inclusion would be anti-dilutive.

Basic earnings per share are based on the weighted-average number of shares of common stock outstanding. Earnings per share, assuming dilution, is based on the weighted-average number of shares of common stock outstanding adjusted for the effects of common stock that may be issued as a result of the following types of potentially dilutive instruments:

-warrants,



**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

-employee stock options, and

-other equity awards, which include long-term incentive awards.

The FASB Topic ASC 260, "*Earnings per Share*," requires the Company to include additional shares in the computation of earnings per share, assuming dilution. The additional shares included in diluted earnings per share represent the number of shares that would be issued if all of the Company's outstanding dilutive instruments were converted into common stock.

Diluted earnings per share are based on the assumption that all dilutive options were converted or exercised. Dilution is computed by applying the treasury stock method. Under this method, options are assumed to be exercised at the time of issuance, and as if funds obtained thereby were used to purchase common stock at the average market price during the period.

**w.**

**Warrants**

The Company evaluates its warrants on an ongoing basis considering the accounting guidance of FASB Topic ASC 825, which establishes standards for issuers of financial instruments with characteristics of both liabilities and equity related to the classification and measurement of those instruments. The warrants are evaluated considering the accounting guidance of FASB Topic ASC 815, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities.

In accordance with accounting guidance FASB Topic ASC 825, the Company accounts for financial instruments as a liability if it embodies an obligation to repurchase the issuer's equity shares, or is indexed to such an obligation, and that requires or may require the issuer to settle the obligation by transferring assets. Freestanding financial instruments are financial instruments that are entered into separately and apart from any of the entity's other financial instruments or equity transactions, or that is entered into in conjunction with some other transaction and is legally detachable and separately exercisable. The liability recorded is fair market value per Black-Scholes option model.

On May 15, 2009, we have issued warrants to purchase 1,071,428 shares of common stock to certain investors, associated with an offering of our common stock. The warrants were recognized at fair value and were recorded as

equity.

On March 25, 2010, we issued warrants to purchase 160,000 shares of our common stock to a certain investor relation service provider. The warrants were recognized at fair value and were recorded as liability.

### **3. ACCOUNTING PRONOUNCEMENTS**

In April 2011, the FASB issued ASU 2011-02 Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring. This ASU clarifies which loan modifications constitute troubled debt restructurings. It is intended to assist creditors in determining whether a modification of the terms of a receivable meets the criteria to be considered a troubled debt restructuring, both for purposes of recording an impairment loss and for disclosure of troubled debt restructurings. For public companies, this ASU is effective for interim and annual periods beginning on or after June 15, 2011, and applies retrospectively to restructurings occurring on or after the beginning of the fiscal year of adoption. Early application is permitted. It is not expected to have a material impact on the Company's consolidated financial statements.

In May 2011, the FASB issued ASU 2011-04 Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. This ASU is the result of joint efforts by the FASB and International Accounting Standards Board ("IASB") to develop a single, converged fair value framework — that is, converged guidance on how (not when) to measure fair value and on what disclosures to provide about fair value measurements. Thus, there are few differences between this ASU and its international counterpart, IFRS 13. While this ASU is largely consistent with existing fair value measurement principles in U.S. GAAP, it expands Topic 820's existing disclosure requirements for fair value measurements and makes other amendments. Many of these amendments were made to eliminate unnecessary wording differences between U.S. GAAP and IFRSs. However, some could change how the fair value measurement guidance in Topic 820 is applied. This ASU is effective for interim and annual periods beginning after December 15, 2011 for public entities. It is not expected to have a material impact on the Company's consolidated financial statements.

## CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES

### NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In June 2011, the FASB issued ASU 2011-05 Comprehensive Income (Topic 220): Presentation of Comprehensive Income, which revises the manner in which entities present comprehensive income in their financial statements. This ASU removes the presentation options in Topic 220 and requires entities to report components of comprehensive income in either (1) a continuous statement of comprehensive income or (2) two separate but consecutive statements. This ASU does not change the items that must be reported in other comprehensive income. For public entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. This ASU does not require incremental disclosures in addition to those required by Topic 250 or any transition guidance. Because the Company is currently adopted to present comprehensive income within the consolidated statements of changes of equity and therefore, it is expected this ASU would change the presentation of comprehensive income in the Company's consolidated financial statements upon its adoption. It is not expected to have a material impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2001-11 Balance Sheet (Topic 210)-Disclosures about Offsetting Assets and Liabilities: The amendments in this Update will enhance disclosures required by U.S. GAAP by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45. This information will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this Update. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. It is not expected to have a material impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2011-12 Comprehensive Income (Topic 220): In order to defer only those changes in Update 2011-05 that relate to the presentation of reclassification adjustments, the paragraphs in this Update supersede certain pending paragraphs in Update 2011-05. The amendments are being made to allow the Board time to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. While the Board is considering the operational concerns about the presentation requirements for reclassification adjustments and the needs of financial statement users for additional information about reclassification adjustments, entities should continue to report 2 reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before Update 2011-05. All other requirements in Update 2011-05 are not affected by this Update, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but consecutive financial statements. Public entities should apply these requirements for fiscal years, and interim periods within those years, beginning after December 15, 2011.

Nonpublic entities should begin applying these requirements for fiscal years ending after December 15, 2012, and interim and annual periods thereafter. It is not expected to have a material impact on the Company's consolidated financial statements.

F-15

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**4. CONCENTRATIONS OF BUSINESS AND CREDIT RISK**

The Company conducts all of its primary trade in the PRC. There can be no assurance that the Company will be able to successfully conduct its trade, and failure to do so would have a material adverse effect on the Company's financial position, results of operations and cash flows. Also, the success of the Company's operations is subject to numerous contingencies, some of which are beyond management's control. These contingencies include general economic conditions, price of raw material, competition, governmental and political conditions, and changes in regulations. Because the Company is dependent on foreign trade in the PRC, the Company is subject to various additional political, economic and other uncertainties. Among other risks, the Company's operations will be subject to risk of restrictions on transfer of funds, domestic and international customs, changing taxation policies, foreign exchange restrictions, and political and governmental regulations.

**(1) Cash**

The Company maintains certain bank accounts in the PRC which are not protected by FDIC insurance or other insurance. Cash balance held in PRC bank accounts to \$15,283,583 and \$27,826,142, as of October 31, 2011 and 2010, respectively. No cash balances were restricted as at October 31, 2011 and 2010.

As of October 31, 2011 and 2010, substantially all of the Company's cash were held by major financial institutions located in the PRC which management believes are of high credit quality.

**(2) Sales and trade receivables**

The Company provides credit in the normal course of business and substantially all customers are located in the PRC. The Company performs ongoing credit evaluations of its customers and maintains allowances for doubtful accounts based on factors surrounding the credit risk of specific customers, historical trends, and other information. Prior to deduction of sales rebates, no individual customer accounted for over 10% of total sales during the year ended October 31, 2011

The Company's products are sold throughout the PRC. For years ended October 31, 2011 and 2010, Botanical anti-depression and nerve-regulation products accounted for 68.0% and 71.1%, respectively, of total sales after sales rebate.

### **(3) Foreign currency**

The Company operates in China, which may give rise to significant foreign currency risks from fluctuations and the degree of volatility of foreign exchange rates between U.S. dollars and the Chinese currency RMB.

### **(4) Dividends**

Payments of dividends may be subject to some restrictions due to the fact that the operating activities are conducted in a subsidiary residing in the PRC.

### **(5) Price control**

The retail prices of certain pharmaceuticals sold in China, primarily those included in the national and provincial Medical Insurance Catalogs are subject to price controls in the form of fixed prices or price ceilings. As such, the retail prices for certain of the Company's pharmaceutical products can be adjusted downward or upward from time to time. Price controls did not have a material impact on the Company's operation during the years ended October 31, 2011 and 2010.

### **(6) Cost of goods sold**

Cost of goods sold is subject to price fluctuations due to various factors beyond the Company's control, including, among other pertinent factors, inflation and changes in governmental regulations and programs. The Company expects cost of goods sold will continue to fluctuate and be affected by inflation in the future. The Company's raw materials are purchased from various independent suppliers, and do not rely on any one supplier.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****5. TRADE RECEIVABLES, NET**

The trade receivables amount included in the consolidated balance sheets as at October 31, 2011 and October 31, 2010 were as follows:

	2011 US\$	2010 US\$
Trade receivables	23,704,241	22,408,628
Less: Sales rebates	(1,681,721 )	(2,141,055 )
Less: Allowance for doubtful accounts	(474,195 )	(453,135 )
Trade receivables, net	21,548,325	19,814,438

**6. OTHER RECEIVABLES, NET**

The other receivables amount included in the consolidated balance sheets as at October 31, 2011 and 2010 were as follows:

	2011 US\$	2010 US\$
Advanced Siberian Ginseng payment	6,631,157	
Other receivables	577,554	569,184
Less: Allowance for doubtful accounts	(385,301 )	(368,190)
Other receivables, net	6,823,410	200,994

The company advanced Siberian Ginseng payment to two of our employees in our DongFanghong branch, Mr. Zhao, Fengwu and Mr. Deng, Fujie, for the purchasing of Siberian Ginseng raw material in the Siberian Ginseng harvest season.

**7. INVENTORY, NET**

The inventory amounts included in the consolidated balance sheets for as at October 31, 2011 and 2010 comprised of:

	2011	2010
	US\$	US\$
Raw materials	2,842,769	1,951,185
Work-in-progress	3,205,862	52,411
Finished goods	1,436,767	707,648
Less: Inventory reserves	(68,678 )	(65,628 )
Inventory, net	7,416,720	2,645,616

**8. PROPERTY AND EQUIPMENT, NET**

Property and equipment and related accumulated depreciation as of October 31, 2011 and 2010 were as follows:



**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

	2011 US\$	2010 US\$
Machinery and equipment	3,710,282	3,545,146
Office equipment and furnishings	66,352	58,006
Motor vehicles	56,759	54,237
	3,833,393	3,657,389
Less: Accumulated depreciation	(2,054,409)	(1,587,929)
Net book value	1,778,984	2,069,460

Depreciation expense for the years ended October 31, 2011 and 2010 was \$383,846 and \$363,567, respectively, of which \$366,483 and \$374,973 were included as a component of cost of goods sold in the respective periods.

No assets were pledged for borrowings as at October 31, 2011 and 2010.

**9. INTANGIBLE ASSETS, NET**

Intangible assets and related accumulated amortization as of October 31, 2011 and 2010 were as follows:

	2011 US\$	2010 US\$
Using right of undergrowth resources	15,685,044	
Product patents	2,509,607	2,398,153
Less: Accumulated amortization	(1,047,951 )	(444,536 )
Intangible assets, net	17,146,700	1,953,617

On January 11, 2011, the company through its wholly own subsidiary, CBP China, entered into an Exclusive Licensing Agreement for Harbin Renhuang Pharmaceutical Co., Ltd. to Use Forest Resources under Yichun Red Star Forestry Bureau (the “Agreement”) with Yichun Red Star Forestry Bureau of Heilongjiang Province (the “Forestry

Bureau”) for 30 years exclusive utilizing right of approximately 6,667 hectares of undergrowth resources, which is rich of wild Siberian Ginseng plant and also includes an approximately 67 hectares of Siberian Ginseng GAP cultivation base. Pursuant to the Agreement, a payment of \$14,116,540 was made to Forestry Bureau in 2011 and with a final payment of \$1,568,504 due in 12 months for a total consideration of \$15,685,044. The exclusive utilizing right was effected and started from February 1, 2011 through January 31, 2042 for total of 30 years of utilizing and cultivation right.

## 10. CONSTRUCTION IN PROGRESS

Construction in progress as of October 31, 2011 and 2010 were as follows:

	2011 US\$	2010 US\$
Ah City Industrial Park phase Two Project	1,937,103	—
Total Construction In Progress	1,937,103	—

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

Plant and production lines currently under development at the Ah City Phase Two are accounted for as construction-in-progress. Construction-in-progress is recorded at historical cost, including development expenditures, professional fees and the interest expenses capitalized during the course of construction for the purpose of financing the project. Upon readiness for use of the project, the cost of construction-in-progress is transferred to property and equipment, at which time depreciation will commence. The Company had no capitalized interest and to date has funded this construction through operations without the use of outside debt financing. As of October 31, 2011, the Company has incurred a total of \$1,937,103 of construction-in-progress. The Ah City Phase Two is expected to be completed in the end of 2013 and these amounts will be reclassified to fixed assets when it is ready to use.

**11. RELATED PARTY TRANSACTIONS**

Due from related parties included in the consolidated balance sheets as at October 31, 2011 and October 31, 2010 comprised of:

	2011	2010
	US\$	US\$
Due from related parties:		
Advances ( 1)	—	28,877
Deposits ( 2)	23,527,566	18,605,935
Total	23,527,566	18,634,812

**(1) Advances**

Mr. Shaoming Li, our chairman, chief executive officer and president, is also chairman and a 50% shareholder of Harbin Renhuang Pharmaceutical Stock Co. Ltd (“Renhuang Stock”).

As of October 31, 2011 and 2010, the Company has a net amount due from Mr. Shaoming Li of \$0 and \$28,877, respectively, which is advance for travelling and business.

## **(2) Deposits**

On October 12, 2009, we entered into a purchase agreement with Renhuang Stock to acquire the land use right, property and plant located at our Ah City Natural and Biopharmaceutical plant for a total consideration of \$25,096,070. Pursuant to the purchase agreement, a payment of \$15,685,044 was made to Renhuang Stock in October 2009 and a payment of \$7,842,522 was made to Renhuang Stock in January 2011, with a final payment of \$1,568,504 due by the date of receiving all the related government transfer documents, at which time title for the assets will be transferred. Accordingly the transaction is considered incomplete as of October 31, 2011.

## **(3) Rental Expenses**

The Company leases property and plant from Renhuang Stock. Rental expenses related to this lease, incurred and expensed to consolidated statements of operations and comprehensive income during the year ended October 31, 2011 and 2010 amounted to \$766,607 and \$367,224, respectively, which were forgiven rental expenses and recognized to account for the rental exemption pursuant to the purchase agreement, and the deposits for the property were reduced accordingly. Under the lease terms, the Company no longer pay rent to Renhuang Stock for the use of the property and plant.

## **12. DEPOSIT**

On April 10, 2010, the Company through its wholly own subsidiary, CBP China, entered into a Purchase Agreement with Hongxiangmingyuan of Heilongjiang Yongtai Company, to acquire two office floors for a total consideration of \$6,017,504. Pursuant to the Purchase Agreement, a payment of \$4,212,253 was made in April 2010 and recorded as deposits on the consolidated balance sheet. Pursuant to the Purchase Agreement, final payment of \$1,805,251 is due by December 20, 2012, at which time title for the assets will be transferred. Accordingly the transaction is considered incomplete as of October 31, 2011. Based on the purchasing agreement between CBP China and Hongxiangmingyuan, the Company does not need to pay any rental fees before the title is transferred. Rental expenses related to this lease, incurred and expensed to consolidated statements of operations and comprehensive income during the year ended October 31, 2011 and 2010 amounted to \$262,174 and \$0, respectively, which were forgiven rental expenses and recognized to account for the rental exemption pursuant to the purchase agreement, and the deposits for the property were reduced accordingly.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****13. DEFERRED TAX ASSETS**

Deferred tax assets as of October 31, 2011 was as follows:

Allowance for doubtful and Inventory provision	Temporary Difference	Income Tax Rate	Deferred Tax Assets
928,174	928,174	0.15	139,226

**14. INCOME TAX EXPENSES**

The Company adopted FIN No. 48 on January 1, 2007. There were no unrecognized tax benefits as of the date of adoption and there is no unrecognized tax benefits included in the balance sheet at October 31, 2011, that would, if recognized, affect the effective tax rate.

The following table reconciles the U.S. statutory rates to the Company's effective tax rate for the years ended October 31, 2011 and 2010:

	The Year ended October 31,	
	2011	2010
US statutory rates	34.00%	34.00%
Foreign tax rate difference	(9.0 )%	(9.0 )%
Income tax holiday	(10.0 )%	(25.0 )%
Tax per financial statements	15.00%	0.00 %

Taxation on profits earned in the PRC has been calculated on the estimated assessable profits for the three and nine months at the rates of taxation prevailing in the PRC in which the Company operates after taking into effect the

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

benefits from any special tax credits or “tax holidays” allowed in the country of operations. If the Company did not have any tax exemption, the effects of the tax per share were as follows:

	The Year ended October 31,	
	2011	2010
	US\$	US\$
Tax savings	3,986,144	4,749,398
Benefit per share:		
Basic	0.11	0.13
Diluted	0.11	0.13

Had the tax exemption not been in place for the years ended October 31, 2011 and 2010, the Company estimates the following pro forma financial statement impact:

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

	The Year ended October 31,	
	2011	2010
	US\$	US\$
Net income as reported	25,919,085	17,868,942
Less Tax savings	(3,986,144 )	(4,749,398 )
Proforma Net income	21,932,941	13,119,544
Proforma Net income per share:		
Basic	0.59	0.35
Diluted	0.58	0.35

**15. EARNINGS PER SHARE**

When calculating diluted earnings per share for common stock equivalents, the Earnings per Share Topic, ASC 260, requires the Company to include the potential shares that would be outstanding if all outstanding stock options or warrants were exercised. This is offset by shares the Company could repurchase using the proceeds from these hypothetical exercises to obtain the common stock equivalent.

The following reconciles the components of the EPS computation:

	Income	Shares	Per
	(Numerator)	(Denominator)	Share
	US\$		Amount
			US\$
For the year ended October 31, 2011:			
Net income	25,919,085		
Basic EPS income available to common shareholders	25,919,085	37,239,536	0.70
Effect of dilutive securities:			
Share options			
Warrants		438,989	
Diluted EPS income available to common shareholders	25,919,085	37,678,525	0.69

For the year ended October 31, 2010:

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

Net income	17,868,942		
Basic EPS income available to common shareholders	17,868,942	37,239,536	0.48
Effect of dilutive securities:			
Share options			
Warrants		538,492	
Diluted EPS income available to common shareholders	17,868,942	37,778,028	0.47

For the year ended October 31, 2011, warrants of 160,000 shares and option of 234,998 shares were excluded from calculation of diluted earnings, because the exercise prices exceeded the average price of the Company's common stock

For the year ended October 31, 2010, warrants of 160,000 shares and option of 70,000 shares were excluded from calculation of diluted earnings, because the exercise prices exceeded the average price of the Company's common stock.



## **CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

### **NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

#### **16. EMPLOYEE BENEFITS**

The full-time employees of the Company's subsidiary that is incorporated in the PRC are entitled to staff welfare benefits, including medical care, welfare subsidies, unemployment insurance and pension benefits. The PRC companies are required to accrue for these benefits based on certain percentages of the employees' salaries in accordance with the relevant regulations, and to make contributions to the state-sponsored pension and medical plans out of the amounts accrued for medical and pension benefits. The total amounts expensed to the consolidated statements of operations and comprehensive income for such employee benefits amounted to approximately \$353,249 and \$401,543 for the years ended October 31, 2011 and 2010, respectively.

#### **17. ASSETS AND LIABILITIES MEASURED AT FAIR VALUE**

On March 25, 2010, the Company issued warrants (the "Warrants") for 160,000 common shares to an investor relation service provider that have an exercise price of \$2.00 per share and a contractual life of 3 years. The terms of the Warrant agreement include the following factors that in accordance with FASB Topic ASC 815, requires that the Warrants be classified at their fair value to liabilities each reporting period.

The holder of the Warrants (the "Holder") is entitled to the benefits of Rule 144 promulgated under the Securities Act of 1933, as amended and any other rule or regulation of the SEC that may at any time permit the Holder to sell securities of the Company to the public without registration. Noncompliance with such rules and regulations could result in the Company having to settle the Warrant obligation in cash.

The exercise price and number of shares issuable upon exercise of the Warrants (the "Warrant Shares") are subject to adjustment for standard dilutive events, including the issuance of common stock, or securities convertible into or exercisable for shares of common stock, that will adversely affect the Holder's rights under the Warrants. There were no dilutive events for the year ended October 31, 2011, which would have resulted in an adjustment to the exercise price or number of Warrant Shares.

At October 31, 2011, the fair value of the Company's warrants liability was \$23,443. The Company used the Black-Scholes valuation model to estimate the fair value of the Warrants. The valuation was based on the assumptions noted in the following table.

Expected volatility	77.10	%
Expected dividends	0	%
Expected term (in years)	1.4	years
Risk-free rate	0.41	%

At October 31, 2011, the Company had no assets measured at fair value and had the following liabilities measured at fair value:

	Fair value measurement		
	Quoted prices in active markets of identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	US\$	US\$	US\$
Warrants liability	—	23,443	—

## 18. PREFERRED STOCK, COMMON STOCK AND EQUITY TRANSACTIONS

### (1) Preferred Stock

The Company's articles of incorporation provide that our board of directors will be authorized to issue from time to time, without further stockholder approval, up to 1,000,000 additional shares of preferred stock in one or more series and to fix or alter the designations, preferences, rights and any qualifications, limitations or restrictions of the shares of each series, including the dividend rights, dividend rates, conversion rights, voting rights, rights of redemption, including sinking fund provisions, redemption price or prices, liquidation preferences and the number of shares constituting any series or designations of any series. Such shares of preferred stock could have preferences over our common stock with respect to dividends and liquidation rights. As at October 31, 2011 and 2010, there is no preferred stock outstanding.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Common Stock and Equity Transactions**

On May 15, 2009, the Company issued an aggregate of 2,142,856 shares of the Company's common stock and 1,071,428 warrants with an exercise price of \$0.875 per share to Allied Merit International Investments, Inc. and Griffin Ventures Ltd. Total consideration of the issuance was \$ 1,500,000.

The fair value of the warrants is estimated on the date of grant using the Black-Scholes option valuation model to be \$496,732. The valuation was based on the assumptions noted in the following table.

Expected volatility	175.80 %
Expected dividends	0 %
Expected term (in years)	3 years
Risk-free rate	1.375 %

The risk-free interest rate is based on the U.S. Treasury yield curve in effect for the expected term of the warrants at the time of grant. The dividend yield on our common stock is assumed to be zero since we do not pay dividends and have no current plans to pay them in the future. The market price volatility of our common stock was based on historical volatility since May 15, 2008. Our methodology is consistent with prior period volatility assumptions. The expected life of the warrants is based upon our anticipated expectations of exercise behavior since no options have been exercised in the past to provide relevant historical data.

**19. OPTION PLAN AND WARRANTS**

Share-based compensation amounted to \$134,865 and \$31,462 in the years ended October 31, 2011 and 2010, respectively.

**(1) 2003 Omnibus Plan**

On February 28, 2003, our board of directors approved the Renhuang Pharmaceuticals, Inc. 2003 Omnibus Securities Plan (the “2003 Plan”), which was approved by our shareholders on April 11, 2003. The 2003 Plan offers selected employees, directors, and consultants an opportunity to acquire our common stock, and serves to encourage such persons to remain employed by us and to attract new employees. The 2003 Plan allows for the award of stock and options, up to 25,000 (after giving effect to the 1-for-30 reverse stock split in 2006) shares of our common stock. On May 1, of each year, the number of shares in the 2003 Securities Plan is automatically adjusted to an amount equal to ten percent of our outstanding stock on October 31, of the immediately preceding year. As of October 31, 2010, the number of shares of common stock outstanding was 37,239,536 making 3,723,954 shares of common stock subject to the 2003 Plan.

On April 13, 2010, an option to purchase 70,000 shares was granted under the 2003 Plan to an independent director that vests on a quarterly basis beginning three months from the date of grant, conditioned upon continued service on such quarterly dates, and has a contractual life of 3 years. The fair value of the option award is estimated on the date of grant using the Black-Scholes option valuation model to be \$171,397, of which \$57,131 and \$31,462 were recorded as compensation expenses for the year ended October 31, 2011 and 2010, respectively. The valuation was based on the assumptions noted in the following table.

Expected volatility	227.9	%
Expected dividends	0	%
Expected term (in years)	3	years
Risk-free rate	1.65	%

The risk-free interest rate is based on the U.S. Treasury yield curve in effect for the expected term of the option at the time of grant. The dividend yield on our common stock is assumed to be zero since we do not pay dividends and have no current plans to pay them in the future. The market price volatility of our common stock was based on historical volatility since April 13, 2009. Our methodology is consistent with prior period volatility assumptions. The expected life of the options is based upon our anticipated expectations of exercise behavior since no options have been exercised in the past to provide relevant historical data.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

On December 14, 2010, we appointed Mr. Weiqiu Dong as our chief financial officer. Base on the employment agreement, Mr. Dong received, on December 14, 2010, an option to purchase 200,000 shares of the Company's b) common stock under the 2003 Omnibus Plan. The option vests 60,000 shares on the first anniversary of the date of grant and 70,000 shares on each of the second and third anniversaries of the date of grant. The Option is conditioned upon continued employment on such date, and has a contractual life of 3 years.

The fair value of the option award is estimated on the date of grant using the Black-Scholes option valuation model to be \$259,251, of which \$76,032 was recorded as compensation expenses for the year ended October 31, 2011 and \$0 was recorded for the year ended October 31, 2010. The valuation was based on the assumptions noted in the following table.

Expected volatility	96.46	%
Expected dividends	0	%
Expected term (in years)	3	years
Risk-free rate	1.06	%

The risk-free interest rate is based on the U.S. Treasury yield curve in effect for the expected term of the option at the time of grant. The dividend yield on our common stock is assumed to be zero since we do not pay dividends and have no current plans to pay them in the future. The market price volatility of our common stock was based on historical volatility since December 13, 2009. Our methodology is consistent with prior period volatility assumptions. The expected life of the options is based upon our anticipated expectations of exercise behavior since no options have been exercised in the past to provide relevant historical data.

c) On October 15, 2011, we entered into an independent director agreement with Mr. Pan, who became our director on October 15, 2011. The agreement provides that Mr. Pan, the Chair of our Audit Committee, will receive (i) a fee of \$2,500 per month, (ii) options to purchase 50,000 shares of common stock under the 2003 Plan, at an exercise price of \$0.80 per share, which is equal to the closing price of the Company's common stock on October 15, 2011, subject to vesting on a quarterly basis (4,166 shares of option to vest on the first 11 quarter anniversaries of the grant and 4,174 shares of option to vest on the 12th quarter anniversary of the grant with the initial 4,166 shares of option vesting to commence on January 15, 2012), and with all vesting conditional upon continued service as a director of the Company as of each such anniversary; and (iii) a reimbursement of out-of pocket expenses incidental to his services on the Board. The agreement expires on the earlier of (i) the date Mr. Pan ceases to be a

member of the board, or (ii) the date of termination of the Agreement.

The fair value of the option award is estimated on the date of grant using the Black-Scholes option valuation model to be \$34,042, of which \$2,837 was recorded as compensation expenses for the year ended October 31, 2011 and \$0 was recorded for the year ended October 31, 2010. The valuation was based on the assumptions noted in the following table.

Expected volatility	127.76 %
Expected dividends	0 %
Expected term (in years)	3 years
Risk-free rate	1.12 %

The risk-free interest rate is based on the U.S. Treasury yield curve in effect for the expected term of the option at the time of grant. The dividend yield on our common stock is assumed to be zero since we do not pay dividends and have no current plans to pay them in the future. The market price volatility of our common stock was based on historical volatility since October 14, 2010. Our methodology is consistent with prior period volatility assumptions. The expected life of the options is based upon our anticipated expectations of exercise behavior since no options have been exercised in the past to provide relevant historical data.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****(2) 2007 Non-Qualified Company Stock Grant and Option Plan**

On March 19, 2007, our board of directors approved the 2007 Non-Qualified Company Stock Grant and Option Plan (the “2007 Plan”). The 2007 Plan is intended to serve as an incentive to and to encourage stock ownership by our directors, officers, and employees, and certain persons rendering service to us, so that such persons may acquire or increase their proprietary interest in our success, and to encourage them to remain in our service. Under the 2007, up to 200,000 shares of our common stock may be subject to options.

On January 13, 2010, an option to purchase 50,000 shares was granted under the 2007 Plan to an employee that vests on the 12-month anniversary of the date of grant, conditioned upon continued employment on such date, and has a contractual life of 3 years. The fair value of the option award is estimated on the date of grant using the Black-Scholes option valuation model to be \$47,527. The valuation was based on the assumptions noted in the following table. The option was forfeited at departure of the employee on August 6, 2010.

Expected volatility	236.5	%
Expected dividends	0	%
Expected term (in years)	3	years
Risk-free rate	1.5	%

The risk-free interest rate is based on the U.S. Treasury yield curve in effect for the expected term of the option at the time of grant. The dividend yield on our common stock is assumed to be zero since we do not pay dividends and have no current plans to pay them in the future. The market price volatility of our common stock was based on historical volatility since January 13, 2009. Our methodology is consistent with prior period volatility assumptions. The expected life of the options is based upon our anticipated expectations of exercise behavior since no options have been exercised in the past to provide relevant historical data.

A summary of option activity under the Company’s option plan as of October 31, 2011 and movement during the twelve months then ended are as follow:

## Options

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

		Weighted average exercise price	Aggregate intrinsic value	Weighted average remaining contractual term
		US\$	US\$	
Outstanding at November 1, 2010	70,000	2.57	171,397	2.45
Granted	250,000	1.88	293,292	4.29
Exercised	-	-	-	-
Forfeited or expired	(35,002 )	2.57	(82,803 )	1.45
Outstanding at October 31, 2011	284,998	1.96	381,886	3.94

A summary of the status of the Company's non-vested options as of October 31, 2011 and movements during the year then ended are as follow:

	Options	Weighted average granted date fair value US\$
Non-vested at November 1, 2010	70,000	1.91
Granted	250,000	1.17
Vested	34,998	1.91
Forfeited or expired	35,002	1.91
Non-vested at October 31, 2011	250,000	1.17

As of October 31, 2011, there was \$214,424 of unrecognized compensation cost related to non-vested share-based compensation granted under the Company's option plan.



**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****(3) Warrants**

As of October 31, 2011, the Company has 1,231,428 warrants outstanding at an average exercise price of \$1.25 per warrant for one share each of the Company's common stock. The warrants expire in 2012 and 2013.

	Warrants	Average exercise Price US\$
Outstanding warrants at November 1, 2010	1,231,428	1.25
Warrants granted	-	-
Exercised	-	-
Expired/cancelled	-	-
Outstanding warrants at October 31, 2011	1,231,428	1.25

Information regarding the warrants outstanding at October 31, 2011 is summarized as below:

Exercise Prices US\$	Warrants outstanding at October 31, 2011		
	Warrants Outstanding	Weighted Average Contractual Life (years)	Weighted Average Exercise Price US\$
0.88	1,071,428	-	-
2.00	160,000	-	-
-	1,231,428	0.65	1.03

**20. STATUTORY RESERVES****(1) Statutory reserves**

Pursuant to the relevant laws and regulations of the PRC, the Company is required to annually transfer 10% of its after tax profit as reported on financial statements prepared under the accounting principles of the PRC to a statutory surplus reserve fund until the balance reaches 50% of the registered share capital. This reserve can be used to make up any losses incurred or to increase share capital. Except for reducing losses incurred, any other application may not result in this reserve balance falling below 25% of the registered capital.

## (2) Public welfare funds

Prior to January 1, 2007, the Company was required each year to transfer 5% of its after tax profit as reported on consolidated financial statements prepared under the accounting principles of the PRC to the public welfare funds. This reserve was restricted to capital expenditure for employees' collective welfare facilities that are owned by the Company. The public welfare funds are not available for distribution to the stockholders (except in liquidation). Once capital expenditures for staff welfare facilities have been made, an equivalent amount must be transferred from the public welfare funds to the discretionary common reserve funds. Due to a change in PRC law, appropriation of profit to the public welfare funds is no longer required.

The reserve funds as of October 31, 2011 and October 31, 2010 were comprised of the following:

	2011	2010
	US\$	US\$
Statutory surplus reserve	3,090,320	3,090,320
Public welfare fund	282,377	282,377
Total	3,372,697	3,372,697

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**21. COMMITMENTS AND CONTINGENCIES**

The Company has various purchase commitments for materials, supplies and services incident to the ordinary conduct of business, generally for quantities required for the Company's business and at prevailing market prices. No material annual loss is expected from these commitments and there are no minimum purchase commitments.

The Company and its subsidiaries are self-insured, and they do not carry any property insurance, general liability insurance, or any other insurance that covers the risks of their business operations. As a result any material loss or damage to its properties or other assets, or personal injuries arising from its business operations would have a material adverse effect on the Company's financial condition and operations.

The Company is not involved in any legal matters arising in the normal course of business. While incapable of estimation, in the opinion of the management, the individual regulatory and legal matters in which it might involve in the future are not expected to have a material adverse effect on the Company's financial position, results of operations, or cash flows.

**(1) Operating lease arrangements**

We currently have no lease agreement with any company.

**(2) Capital commitments**

On October 12, 2009, we entered into a purchase agreement with Harbin Renhuang Pharmaceutical Stock Co. Ltd ("Renhuang Stock") to acquire the land use right, property and plant located at our Ah City Natural and Biopharmaceutical plant for a total consideration of \$25,096,070. Pursuant to the purchase agreement, a payment of \$15,685,044 was made to Renhuang Stock in October 2009 and a payment of \$7,842,522 was made to Renhuang Stock in January 2011, with a final payment of \$1,568,504 will be paid once we received all the related title transfer document from local government, at which time title for the assets will be transferred. According to the agreement, we

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

were exempted from lease payments for the underlying assets starting from May 1, 2010.

On April 10, 2010, CBP China entered into a Purchase Agreement with Hongxiangmingyuan of Heilongjiang Yongtai Company, to acquire two office floors for a total consideration of \$6,017,504. Pursuant to the Purchase Agreement, a payment of \$4,212,253 was made in April 2010 and recorded as deposits on the consolidated balance sheet. Pursuant to the Purchase Agreement, final payment of \$1,805,251 is due by December 20, 2012, at which time title for the assets will be transferred. Accordingly the transaction is considered incomplete as at October 31, 2011.

Name of Fixed Asset	Purchase Date	Prepaid Amount US\$	Remaining Amount US\$	Total Amount US\$
Ah City Pharmaceutical Plant	October, 2009	23,527,566	1,568,504	25,096,070
Two Office Floor	April, 2010	4,212,253	1,805,251	6,017,504
Total		27,739,819	3,373,755	31,113,574

In January, 2011, CBP China started its Ah City Phase Two project for Siberian Ginseng products development and industrialization and entered into a Construction and Engineering Design Contract (the "Contract") with Heilongjiang Medical Architecture Design Institute (the "Institute") for architectural design. A few payments have been made to Institute and relevant local government departments for design and start up fees and we recorded \$1,937,103 as Construction in progress for Ah City Phase Two project. The estimated total investment for Ah City Phase Two is \$18,822,053. In anticipation of the project proceeding, we expect to pay approximately \$9,356,129 in our fiscal year 2012 and \$7,528,821 in our fiscal year 2013. The project is anticipated to be finished in 2013.

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

Name of Construction in Progress	Started Date	Paid Amount US\$	Remaining Amount US\$	Projected Total Amount US\$
Ah City Phase Two(Siberian Ginseng Product Industrialization)	August, 2011	1,937,103	16,884,950	18,822,053

On January 11, 2011, CBP China entered into an Exclusive Licensing Agreement for Harbin Renhuang Pharmaceutical Co., Ltd. to Use Forest Resources under Yichun Red Star Forestry Bureau (the “Agreement”) with Yichun Red Star Forestry Bureau of Heilongjiang Province (the “Forestry Bureau”) for 30 years exclusive utilizing right of approximately 6,667 hectares of undergrowth resources, which is rich in wild Siberian Ginseng plant and also includes approximately 67 hectares of Siberian Ginseng GAP cultivation base in Heilongjiang Province. Pursuant to the Agreement, a payment of \$7,842,522 was made to Forestry Bureau in January 2011, second payment of \$6,274,018 was made in October, 2011 and with a final payment of \$1,568,504 due in 12 months from the date of Agreement approved by local government authorities for a total consideration of \$15,685,044. Siberian Ginseng is a plant with medically-established anti-depressant and mood regulation qualities and is also an active ingredient in our market-leading line of all-natural anti-depressant medications. We will be responsible for continued maintenance and protection of wild resources to make this area a professional Siberian Ginseng base.

In the fourth quarter of our fiscal year 2011, we purchased five patents listed as the following table.

Name of Intangible Assets	Purchase Date	Paid Amount US\$	Remaining Amount US\$	Total Amount US\$
Patent of Ingredients and preparation for Parkinson Drug	August, 2011	1,348,914	1,348,914	2,697,828
Patent of Ingredients and preparation for XiangDousu	August, 2011	1,333,229	1,333,229	2,666,458
Patent of Mudouye Extract	September, 2011	1,882,205	1,882,205	3,764,410
Patent of Hongdoushan Extract	September, 2011	2,368,442	2,368,442	4,736,884
Patent of Ingredients and preparation for Jizhi Pills	October, 2011	2,117,481	2,117,481	4,234,962
Yichun Undergrowth Resource Exclusive Using right	January, 2011	14,116,540	1,568,504	15,685,044
Total		23,166,811	10,618,775	33,785,586

Edgar Filing: China Botanic Pharmaceutical - Form 10-K

On February 1, 2011, the Company entered into an advertising contract with Harbin Weishi Advertising Company to advertise its products from February 1, 2011 to January 31, 2012 as shown on the following table.

Advertising Contract	Contract Date	Paid Amount US\$	Remaining Amount US\$	Total Amount US\$
Harbin TV Weishi Advertising Company	February, 2011	4,587,875	1,529,292	6,117,167

As of October 31, 2011, the Company has capital commitments for purchase of Ah City Nature and Pharmaceutical Plant, two office floors, undergrowth resources right, five patents, advertising contract and Ah City Phase Two construction in progress of approximately \$32,406,772. The amounts to be paid in the future years are as follows:

Calendar Year	Payment for properties
2012	\$ 23,072,700
2013	9,334,072
2014	—
2015	—
2016	—
Thereafter	—
Total	\$ 32,406,772

**CHINA BOTANIC PHARMACEUTICAL INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**22. SUBSEQUENT EVENT**

On November 22, 2011, the company withdrew its Registration Statement on Form S1 which was filed on December 06, 2010. The Company has determined, because of unfavorable market conditions, not to proceed with the registration and sale of its common stock as contemplated by the Registration Statement. The Registration Statement has not been declared effective and no securities have been sold pursuant to the Registration Statement.

On January 6, 2012, the Board of Directors of China Botanic Pharmaceutical Inc. (the “Company”) approved an amendment and restatement of the Company’s bylaws (the “Amended and Restated Bylaws”) pursuant to the authority granted by Section 2 of Article V of the Company’s bylaws. The Amended and Restated Bylaws replace the Company’s current bylaws (“Old Bylaws”). The Company’s Board of Directors (the “Board”) believes the Amended and Restated Bylaws are in the best interests of the Company’s shareholders.