

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 20-F

(Mark One)

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

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2021
OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____.
OR

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

Date of event requiring this shell company report

For the transition period from _____ to _____

Commission file number: 001-38639

111, Inc.

(Exact name of Registrant as specified in its charter)

N/A

(Translation of Registrant's name into English)

Cayman Islands

(Jurisdiction of incorporation or organization)

**3-5/F, No.295 ZuChongZhiRoad,
Pudong New Area
Shanghai, 201203**

The People's Republic of China

(Address of principal executive offices)

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Shanghai, 201203**

The People's Republic of China

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

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

Title of each class	Trading Symbol	Name of each exchange on which registered
American depositary shares (one American depositary share representing two Class A ordinary shares, par value US\$0.00005 per share)	YI	The Nasdaq Stock Market LLC (The Nasdaq Global Market)
Class A ordinary shares, par value US\$0.00005 per share*		The Nasdaq Stock Market LLC (The Nasdaq Global Market)

* Not for trading, but only in connection with the listing on the Nasdaq Global Market of American depositary shares.

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Securities registered or to be registered pursuant to Section 12(g) of the Act:

Not Applicable

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

Not Applicable

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

As of December 31, 2021, there were 166,148,486 ordinary shares outstanding, par value US\$0.00005 per share, being the sum of 94,148,486 Class A ordinary shares and 72,000,000 Class B ordinary shares.

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

Yes No

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

Yes No

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 every Interactive Data File required to be submitted 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 such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or an emerging growth company. See definition of "large accelerated filer," "accelerated filer," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer Non-accelerated Filer Emerging growth company

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards† provided pursuant to Section 13(a) of the Exchange Act.

† The term "new or revised financial accounting standard" refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012.

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report.

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

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

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

Item 17 Item 18

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

Yes No

(APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PAST FIVE YEARS)

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes No

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INTRODUCTION

Unless otherwise indicated or the context otherwise requires, all information in this annual report reflects the following:

- “1 Clinic” refers to our internet hospital;
- “1 Pharmacy”, previously known as “1 Drug Mall”, refers to our online wholesale pharmacy;
- “1 Medicine Marketplace”, previously known as “1 Drugstore” refers to our online retail pharmacy;
- “ADSs” refer to American depository shares, each of which represents two Class A ordinary shares;
- “China” or the “PRC” refers to the People’s Republic of China, excluding, for the purposes of this annual report only, Hong Kong, Macau and Taiwan;
- “DTP” refers to direct to patient;
- “GMV” refers to the total value of all orders shipped for products sold under our direct sales model, net of returns, plus the total value of all orders shipped for products sold on our marketplace by our marketplace sellers, inclusive of returns, during the specified period;
- “marketplace sellers” refer to third-party merchants on our 1 Medicine Marketplace and 1 Pharmacy, which include distributors and resellers that sell products through our online retail pharmacy or online wholesale pharmacy under our marketplace model;
- “medical professionals” refer to doctors, pharmacists and medical assistants;
- “New Retail” refers to the seamless integration of our online retail pharmacy and offline pharmacy network by leveraging our smart supply chain and cloud-based solutions to improve the efficiency throughout the value chain;
- “pharmaceutical companies” refer to manufacturers of pharmaceutical and other health and wellness products;
- “pharmacies” refer to independent pharmacies, pharmacy chains and in-house pharmacies within clinics and private hospitals;
- “RMB” or “Renminbi” refers to the legal currency of China;
- “shares” or “ordinary shares” refers to our ordinary shares comprising Class A and Class B ordinary shares, par value US\$0.00005 per share;
- “SKU” refers to stock keeping unit;
- “smart supply chain” refers to a supply chain built upon a technology infrastructure that is designed to analyze massive amounts of data to facilitate the customization, productivity and efficiency needed in the New Retail era. Our smart supply chain consists of multiple components, including our fulfillment infrastructure, cloud-based inventory management and our supply chain management;
- “suppliers” refer to distributors and pharmaceutical companies from whom we source our products for our direct sales model;
- “U.S. GAAP” refers to generally accepted accounting principles in the United States;
- “US\$,” “U.S. dollars,” “\$,” or “dollars” refers to the legal currency of the United States; and
- “we,” “us,” “our company,” “our,” or “111” refers to 111, Inc., its subsidiaries and, in the context of describing our consolidated financial information, business operations and operating data for the periods preceding the termination of the VIE structure, the previous variable interest entities.

Our reporting currency is the Renminbi because our business is mainly conducted in China and all of our revenues are denominated in Renminbi. However, periodic reports made to shareholders will include current period amounts translated into U.S. dollars using the then-current exchange rates, for the convenience of the readers. The conversion of RMB into U.S. dollars in this annual report is based on the exchange rate set forth in the H.10 statistical release of the Federal Reserve Board. Unless otherwise noted, all translations from RMB to U.S. dollars and from U.S. dollars to RMB in this annual report were made at a rate of RMB6.3726 to US\$1.00, the exchange rate on December 30, 2021 set forth in the H.10 statistical release of the Federal Reserve Board. We make no representation that any RMB or U.S. dollar amounts could have been, or could be, converted into U.S. dollars or RMB, as the case may be, at any particular rate, or at all.

FORWARD-LOOKING INFORMATION

This annual report on Form 20-F contains forward-looking statements that involve risks and uncertainties. All statements other than statements of current or historical facts are forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from those expressed or implied by the forward-looking statements.

You can identify these forward-looking statements by terminology such as "may," "will," "expect," "anticipate," "aim," "estimate," "intend," "plan," "believe," "likely to" or other similar expressions. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. These forward-looking statements include, but are not limited to:

- our goals and strategies;
- our future business development, financial condition and results of operations;
- expected changes in our revenues, costs or expenditures;
- our expectations regarding demand for and market acceptance of our services;
- competition in our industry; and
- government policies and regulations relating to our industry.

We would like to caution you not to place undue reliance on these forward-looking statements and you should read these statements in conjunction with the risk factors disclosed in "Item 3D. Key Information—Risk Factors." Those risks are not exhaustive. We operate in a rapidly evolving environment. New risks emerge from time to time and it is impossible for our management to predict all risk factors, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ from those contained in any forward-looking statement. We do not undertake any obligation to update or revise the forward-looking statements except as required under applicable law.

PART I

Item 1. Identity of Directors, Senior Management and Advisers

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

111, Inc. is a Cayman Islands holding company and currently conducts its operations in China through its PRC subsidiaries. Investors in our ADSs are purchasing equity securities of a Cayman Islands holding company rather than equity securities issued by our operating subsidiaries.

We historically operated our business through contractual arrangements with variable interest entities, or VIEs, based in the PRC, namely Guangdong Yihao Pharmacy Co., Ltd. (“Yihao Pharmacy”), Guangdong Yihao Pharmaceutical Chain Co., Ltd. (“Yihao Pharmaceutical Chain”) and Shanghai Yaowang E-Commerce Co., Ltd. (“Shanghai Yaowang”) in which we did not directly own any equity interests. Shanghai Yaowang is directly wholly owned by Yihao Pharmaceutical Chain, which is directly wholly owned by Yihao Pharmacy. In February 2022, we terminated the contractual arrangements between 1 Pharmacy Technology and the VIEs, and Mr. Yue Xuan and Ms. Jing Liu, who were the shareholders of Yihao Pharmacy, transferred their equity interests in Yihao Pharmacy to 1 Pharmacy Technology. Following such termination and share transfer, all of the VIEs became our subsidiaries in which we hold direct equity ownership interests. For additional information, see “Item 4. Information on the Company—A. History and Development of the Company.” As used in this annual report, “we,” “us,” “our company,” “our,” or “111” refers to 111, Inc. and its subsidiaries, and, in the context of describing our consolidated financial information, business operations and operating data for the periods preceding the termination of the foregoing contractual arrangements, the previous VIEs.

We face various legal and operational risks and uncertainties as a company based in and primarily operating in China. The PRC government has significant authority to exert influence on the ability of a China-based company, like us, to conduct its business, accept foreign investments or be listed on a U.S. stock exchange. For example, we face risks associated with regulatory approvals of offshore securities offerings, anti-monopoly regulatory investigations and actions, cybersecurity and data privacy compliance, as well as the lack of inspection from the U.S. Public Company Accounting Oversight Board, or PCAOB, on our auditors (which may potentially lead to the delisting of ADSs from the U.S. market). The PRC government may also intervene with or influence our operations as it deems appropriate to further regulatory, political and societal goals. The PRC government has recently published new policies that affected our industry and we cannot rule out the possibility that it will in the future further release regulations or policies regarding our industry that could adversely affect our business, financial condition and results of operations. Any such action, once taken by the PRC government, could cause the value of such securities to significantly decline or in extreme cases, become worthless.

Implication of the Holding Foreign Companies Accountable Act

The Holding Foreign Companies Accountable Act, or the HFCAA, was enacted on December 18, 2020. The HFCAA states if the SEC determines that we have filed audit reports issued by a registered public accounting firm that has not been subject to inspection by the PCAOB for three consecutive years beginning in 2021, the SEC shall prohibit our shares or ADSs from being traded on a national securities exchange or in the over-the-counter trading market in the United States. On December 16, 2021, PCAOB issued the HFCAA Determination Report, according to which our auditors are subject to the determinations. Our auditor, the independent registered public accounting firm that issues the audit report included elsewhere in this annual report, as an auditor of companies that are traded publicly in the United States and a firm registered with the PCAOB, is subject to laws in the United States pursuant to which the PCAOB conducts regular inspections to assess its compliance with the applicable professional standards. Since our auditor is located in China, a jurisdiction where the PCAOB has been unable to conduct inspections without the approval of the PRC authorities, our auditor is currently not inspected by the PCAOB. Final rules implementing the submission and disclosure requirements in the HFCAA were adopted by the SEC on December 2, 2021. The delisting of the ADSs, or the threat of their being delisted, may materially and adversely affect the value of your investment. The PCAOB is currently unable to inspect our auditors in relation to their audit work performed for our financial statements and inability of the PCAOB to conduct inspections over our auditors deprives our investors with the benefits of such inspections. On June 22, 2021, the U.S. Senate passed a bill, which would reduce the number of consecutive non-inspection years required for triggering the prohibitions under the HFCAA from three years to two. On February 4, 2022, the U.S. House of Representatives passed a bill, which contained, among other things, an identical provision. If this provision is enacted into law and the number of consecutive non-inspection years required for triggering the prohibitions under the HFCAA is reduced from three years to two, then our shares and ADSs could be prohibited from trading in the United States in 2023. For the details of the risks associated with the enactment of the HFCAA, see “Item 3. Key Information—3.D. Risk Factors—Risks Related to Doing Business in China—Our ADSs may be delisted and our ADSs and Class A ordinary shares may be prohibited from trading in the over-the-counter market under the Holding Foreign Companies Accountable Act, or the HFCAA, if the PCAOB is unable to inspect or fully investigate auditors located in China. On December 16, 2021, PCAOB issued the HFCAA Determination Report, according to which our auditor is subject to the determinations that the PCAOB is unable to inspect or investigate completely. Under the current law, delisting and prohibition from over-the-counter trading in the U.S. could take place in 2024. If this happens there is no certainty that we will be able to list our ADSs or Class A ordinary shares on a non-U.S. exchange or that a market for our ADSs or Class A ordinary shares will develop outside of the U.S. The delisting of our ADSs, or the threat of their being delisted, may materially and adversely affect the value of your investment.”

Transfer of Funds and Other Assets through Our Organization

111, Inc. has not previously declared or paid any cash dividend or dividend in kind, and has no plan to declare or pay any dividends in the near future on our shares or the ADSs representing our ordinary shares. We currently intend to retain most, if not all, of our available funds and any future earnings to operate and expand our business. See “Item 8.—Financial Information—A. Consolidated Statements and Other Financial Information—Dividend Policy.”

Prior to the termination of the VIE structure in February 2022, we were not able to make direct capital contribution to the VIEs because we controlled the VIEs through contractual arrangements, as opposed to equity ownership. Instead, prior to the termination of the VIE structure in February 2022, 111, Inc. and its subsidiaries (i) have transferred cash to the VIEs as working capital support; and (ii) made payments to, or received payments from, the VIEs for intra-group trades of goods. In 2019, 2020 and 2021, 111, Inc. and its subsidiaries made net payments as working capital support to the VIEs of RMB195.1 million, RMB532.3 million and RMB760.3 million, respectively. In addition, the VIEs received net payments from 111, Inc. and its subsidiaries of RMB30.5million and RMB140.1 million, respectively, in 2019 and 2021 and made net payment of RMB78.5 million to 111, Inc. and its subsidiaries in 2020, as part of the foregoing intra-group trades of goods.

As of the date of this annual report, through its intermediate holding company, 111, Inc. had made cumulative capital contributions of US\$342.5 million to 111, Inc.’s PRC subsidiaries. These funds have been used by such PRC subsidiaries mainly for their business operations.

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Prior to the termination of the VIE structure in February 2022, the VIEs might transfer cash to 1 Pharmacy Technology by paying service fees pursuant to the contractual arrangements through which we controlled the VIEs. For the years ended December 31, 2019, 2020 and 2021, the payment of service fees from the VIEs to 1 Pharmacy Technology amounted to nil, RMB112.6 million and RMB728.5 million, respectively. There were no other assets transferred between the VIEs, on one hand, and 111, Inc. and its subsidiaries, on the other hand, in 2019, 2020 and 2021. In 2019, 2020 and 2021, no dividends or distributions were made to 111, Inc. by its subsidiaries.

For the purpose of illustration, the below table reflects the hypothetical taxes that might be required to be paid within China, assuming that: (i) we have taxable earnings, and (ii) we determine to pay a dividend in the future:

	Taxation Scenario Statutory Tax and Standard Rates
Hypothetical pre-tax earnings in the PRC subsidiaries (other than 1 Pharmacy Technology) ⁽¹⁾	100.00
Tax on earnings at statutory rate of 25% at the 1 Pharmacy Technology level ⁽²⁾	(25.00)
Less: net earnings impact of non-controlling shareholders	(10.33)
Net earnings available for distribution from 1 Pharmacy Technology to Yao Wang Corporation Limited ⁽³⁾	64.67
Withholding tax at tax treaty rate of 10% ⁽⁴⁾	(6.47)
Amount to be distributed as dividend at the Yao Wang Corporation Limited level and net distribution to 111, Inc.	58.2

Notes:

(1) For purposes of this example, the tax calculation has been simplified. The hypothetical book pre-tax earnings amount, not considering book to tax adjustment, is assumed to equal Chinese taxable income.

(2) Certain of our subsidiaries qualify for a 15% preferential income tax rate in China. However, such rate is subject to qualification or temporary in nature and may not be available in future when distributions are actually paid. For purposes of this hypothetical example, the table above reflects a maximum tax scenario under which the full statutory rate would be effective.

(3) Yao Wang Corporation Limited holds 86.23% equity of 1 Pharmacy Technology.

(4) China's Enterprise Income Tax Law imposes a withholding income tax of 10% on dividends distributed by a Foreign Invested Enterprise to its immediate holding company outside of Mainland China. A lower withholding income tax rate of 5% is applied if the Foreign Invested Enterprise's immediate holding company is registered in Hong Kong or other jurisdictions that have a tax treaty arrangement with Mainland China, subject to a qualification review at the time of the distribution. For purposes of this hypothetical example, the table above assumes a maximum tax scenario under which the full withholding tax would be applied.

Restrictions on Foreign Exchange and the Ability to Transfer Cash between Entities, Across Borders and to U.S. Investors

In the future, if and when we become profitable, 111, Inc.'s ability to pay dividends, if any, to its shareholders and ADS holders and to service any debt it may incur will depend upon dividends paid by our PRC subsidiaries. Under PRC laws and regulations, our PRC subsidiaries are subject to certain restrictions with respect to paying dividends or otherwise transferring any of their net assets offshore to 111, Inc. In particular, under the current effective PRC laws and regulations, dividends may be paid only out of distributable profits. Distributable profits are the net profit as determined under PRC GAAP, less any recovery of accumulated losses and appropriations to statutory and other reserves required to be made. Each of our PRC subsidiaries is required to set aside at least 10% of its after-tax profits each year, after making up previous years' accumulated losses, if any, to fund certain statutory reserve funds, until the aggregate amount of such a fund reaches 50% of its registered capital. As a result, our PRC subsidiaries may not have sufficient distributable profits to pay dividends to us in the near future.

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Furthermore, if certain procedural requirements are satisfied, the payment of current account items, including profit distributions and trade and service related foreign exchange transactions, can be made in foreign currencies without prior approval from State Administration of Foreign Exchange (the “SAFE”) or its local branches. However, where RMB is to be converted into foreign currency and remitted out of China to pay capital expenses, such as the repayment of loans denominated in foreign currencies, approval from or registration with competent government authorities or its authorized banks is required. The PRC government may take measures at its discretion from time to time to restrict access to foreign currencies for current account or capital account transactions. If the foreign exchange control system prevents us from obtaining sufficient foreign currencies to satisfy our foreign currency demands, we may not be able to pay dividends in foreign currencies to our offshore intermediary holding companies or ultimate parent company, and therefore, our shareholders or investors in our ADSs. Further, we cannot assure you that new regulations or policies will not be promulgated in the future, which may further restrict the remittance of RMB into or out of the PRC. We cannot assure you, in light of the restrictions in place, or any amendment to be made from time to time, that our current or future PRC subsidiaries will be able to satisfy their respective payment obligations that are denominated in foreign currencies, including the remittance of dividends outside of the PRC. If any of our subsidiaries incurs debt on its own behalf in the future, the instruments governing such debt may restrict its ability to pay dividends to 111, Inc. In addition, our PRC subsidiaries are required to make appropriations to certain statutory reserve funds, which are not distributable as cash dividends except in the event of a solvent liquidation of the companies.

For PRC and United States federal income tax consideration of an investment in the ADSs, see “Item 10. Additional Information—E. Taxation.”

Permissions Required from the PRC Authorities for Our Operations

We conduct our business primarily through our subsidiaries in China. Our operations in China are governed by PRC laws and regulations. As of the date of this annual report, except as disclosed in this annual report, our PRC subsidiaries have obtained the requisite licenses and permits from the PRC government authorities that are material for the business operations of our subsidiaries in China, including, among others, the EDI License, Pharmaceutical Operation License, the Record-Filing Certificate for Business Operations of Class II Medical Devices, Permit for Business Operations of Class III Medical Devices, Internet Drug Information Service Qualification Certificate, License for Practicing of Medical Institutions, and Food Business License. Given the uncertainties of interpretation and implementation of relevant laws and regulations and the enforcement practice by relevant government authorities, we may be required to obtain additional licenses, permits, filings or approvals for the functions and services of our platform in the future. For more detailed information, see “Item 3. Key Information—D. Risk Factors—Risks Related to Our Business and Industry—Any lack of requisite approvals, licenses or permits applicable to our business, or any non-compliance with relevant laws and regulations, may have a material and adverse effect on our business, financial condition, results of operations and prospects.”

Furthermore, under current PRC laws, regulations and regulatory rules, we may be required to obtain permissions from the China Securities Regulatory Commission, or the CSRC, and may be required to go through cybersecurity review by the Cyberspace Administration of China, or the CAC, in connection with any future offering and listing in an overseas market. As of the date of this annual report, we have not been subject to any cybersecurity review made by the CAC. If we fail to obtain the relevant approval or complete other review or filing procedures for any future offshore offering or listing, we may face sanctions by the CSRC or other PRC regulatory authorities, which may include fines and penalties on our operations in China, limitations on our operating privileges in China, restrictions on or prohibition of the payments or remittance of dividends by our subsidiaries in China, restrictions on or delays to our future financing transactions offshore, or other actions that could have a material and adverse effect on our business, financial condition, results of operations, reputation and prospects, as well as the trading price of our ADSs.

The PRC government has recently indicated an intent to exert more oversight and control over offerings that are conducted overseas and/or foreign investment in China-based issuers. For more detailed information, see “Item 3. Key Information—D. Risk Factors—Risks Related to Our Corporate Structure—The approval, filing or other requirements of the China Securities Regulatory Commission or other PRC government authorities may be required under PRC law in connection with our issuance of securities overseas.”

A. [Reserved]

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Below please find a summary of the principal risks and uncertainties we face, organized under relevant headings.

Risks Related to Our Business and Industry

- We are subject to extensive and evolving regulatory requirements, non-compliance with which, or changes in which, may materially and adversely affect our business and prospects.
- Our business, financial condition and results of operations may be materially and adversely affected if we are unable to compete effectively in the PRC general health and wellness market, and we may fail to sufficiently and promptly respond to rapid changes in government regulations, treatment of diseases and customer preferences.
- We may not be able to manage the growth of our business and our expansion plans and operations or implement our business strategies on schedule or within our budget, or at all.
- We have incurred operating losses in the past, and may not be able to achieve or maintain profitability in the future.
- Our pharmaceutical retail and wholesale businesses are subject to a variety of risks, which may have a material and adverse effect on our business, financial condition and results of operations.
- Our business generates and processes a large amount of data, and complying with evolving laws and regulations regarding cybersecurity, information security, privacy and data protection and other related laws and requirements may be expensive and may force us to make adverse changes to our business. Many of these laws and regulations are subject to changes and uncertain interpretations, and any failure to comply with these laws and regulations could result in negative publicity, legal proceedings, suspension or disruption of operations, increased cost of operations, or otherwise harm our business.
- Our failure to properly manage various participants in our ecosystem may materially and adversely affect our business.
- Any lack of requisite approvals, licenses or permits applicable to our business, or any non-compliance with relevant laws and regulations, may have a material and adverse effect on our business, financial condition, results of operations and prospects.
- We may become subject to product liability and medical liability claims, which could cause us to incur significant expenses and be liable for significant damages if not covered by insurance.
- If we are unable to implement our strategy to expand our PRC operations by completing an initial public offering and listing on the STAR Market, our ability to strengthen our market position and operations in the PRC could be materially impaired. Even if we complete the STAR Market listing, we may not achieve the results contemplated by our business strategy and our strategy for growth in the PRC may not result in increase in the trading price of our ADSs.

Risks Related to Doing Business in China

- Changes in China's economic, political or social conditions or government policies could have a material adverse effect on our business and results of operations.

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- Uncertainties in the interpretation and enforcement of PRC laws and regulations and sudden or unexpected changes in policies, laws and regulations in China could limit the legal protections available to us.
- The approval, filing or other requirements of the China Securities Regulatory Commission or other PRC government authorities may be required under PRC law in connection with our issuance of securities overseas.
- We may be adversely affected by the complexity, uncertainties and changes in PRC regulation of pharmaceutical and healthcare industry and internet-related businesses, and any lack of requisite approvals, licenses or permits applicable to our business may have a material adverse effect on our business and results of operations.
- We rely on dividends and other distributions on equity paid by our PRC subsidiaries to fund any cash and financing requirements we may have, and any limitation on the ability of our PRC subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our business.
- Our ADSs may be delisted and our ADSs and Class A ordinary shares may be prohibited from trading in the over-the-counter market under the Holding Foreign Companies Accountable Act, or the HFCAA, if the PCAOB is unable to inspect or fully investigate auditors located in China. On December 16, 2021, PCAOB issued the HFCAA Determination Report, according to which our auditor is subject to the determinations that the PCAOB is unable to inspect or investigate completely. Under the current law, delisting and prohibition from over-the-counter trading in the U.S. could take place in 2024. If this happens there is no certainty that we will be able to list our ADSs or Class A ordinary shares on a non-U.S. exchange or that a market for our ADSs or Class A ordinary shares will develop outside of the U.S. The delisting of our ADSs, or the threat of their being delisted, may materially and adversely affect the value of your investment.

Risks Related to American Depository Shares

- The trading price for the ADSs may be volatile.
- Techniques employed by short sellers may drive down the trading price of the ADSs.
- Our dual-class share structure with different voting rights will limit your ability to influence corporate matters and could discourage others from pursuing any change of control transactions that holders of our Class A ordinary shares and ADSs may view as beneficial.
- The dual-class structure of our ordinary shares may adversely affect the trading market for our ADSs.

Risks Related to Our Business and Industry

We are subject to extensive and evolving regulatory requirements, non-compliance with which, or changes in which, may materially and adversely affect our business and prospects.

Due to the complex nature of our business, we are subject to legal and regulatory requirements of multiple industries in the PRC. These industries primarily include internet, healthcare, internet healthcare and pharmaceutical retail and wholesale industries.

Various regulatory authorities of the PRC government are empowered to promulgate and implement regulations governing broad aspects of the internet and healthcare industries. In respect of the healthcare industry, in particular, any violation of the relevant laws, rules and regulations may result in harsh penalties and, under certain circumstances, lead to criminal prosecution.

Meanwhile, the regulations of both the internet industry and its internet healthcare sector are relatively new and evolving, and their interpretation and enforcement involve significant uncertainty. As a result, under certain circumstances, it may be difficult to determine what actions or omissions would be deemed in violation of applicable laws and regulations. These uncertainties entail risks that may materially and adversely affect our business prospects. Due to the uncertainty and complexity of the regulatory environment, we cannot assure you that future laws and regulations would not render our operations non-compliant or that we would always be in full compliance with applicable laws and regulations. Compliance with future laws and regulations may require us to change our business models and practices at an undeterminable and possibly significant financial cost. These additional monetary expenditures

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may increase future overhead, which may, in turn, have a material adverse effect on our business, financial condition and results of operations.

Furthermore, the introduction of new services and products may require us to comply with additional, yet undetermined, laws and regulations. Compliance may require obtaining appropriate permits, licenses or certificates as well as expending additional resources to monitor developments in the relevant regulatory environment. The failure to adequately comply with these future laws and regulations may delay, or possibly prevent, some of our products or services from being offered to users, which may have a material adverse effect on our business, financial condition and results of operations.

The pharmaceutical retail and wholesale industry in China is subject to extensive government regulation and supervision as well as monitoring by various government authorities. Certain other laws, rules and regulations may affect the pricing, demand and distribution of pharmaceutical products, such as those relating to procurement, prescription and dispensing of drugs by hospitals and other medical institutions, retail pharmacy, government funding for private healthcare and medical services, and the inclusion of products in the drugs catalogs for national basic medical insurance, on-the-job injury insurance and maternity insurance promulgated by the Ministry of Human Resources and Social Security of the People's Republic of China, or the MOHRSS. In addition, the pharmaceutical manufacturing, pharmaceutical distribution, pharmaceutical retail, healthcare services and medical device industries in China are each subject to extensive and changing government regulations and supervision. Any unfavorable regulatory changes in these industries may also increase our compliance burden and materially and adversely affect our business, profitability and prospects.

Our business, financial condition and results of operations may be materially and adversely affected if we are unable to compete effectively in the PRC general health and wellness market, and we may fail to sufficiently and promptly respond to rapid changes in government regulations, treatment of diseases and customer preferences.

The PRC general health and wellness market is highly competitive. Our key competitors include pharmaceutical retail companies including traditional offline pharmacies, and online platforms, as well as B2B platforms and traditional pharmaceutical distributors, and companies that offer internet healthcare services. These companies may have substantially greater financial, technical, research and development, marketing, distribution, retail and other resources than we do. They may also have longer operating histories, a larger customer base or broader and deeper market coverage. Furthermore, when we expand into other markets, we will face competition from new competitors, domestic or foreign, who may also enter markets where we currently operate.

In addition, many operators in the healthcare industry have consolidated in recent years to create larger healthcare enterprises with greater bargaining power, which has resulted in greater pricing pressures. If this consolidation trend continues, it could give the resulting enterprises even greater bargaining power, which may lead to further competitive pressure. New partnerships and strategic alliances in the healthcare industry also can alter market dynamics and adversely impact our businesses and competitive positioning.

The technologies that we and our competitors employ are evolving rapidly, and new developments frequently result in price competition, product obsolescence and altered market landscape. Any significant increase in competition may have a material adverse effect on our revenue and profitability as well as on our business and prospects. We cannot assure you that we will be able to continually distinguish our products and services from our competitors', preserve and improve our relationships with various participants in the healthcare value chain, or increase or even maintain our existing market share. We may lose market share, and our financial condition and results of operations may deteriorate significantly if we fail to compete effectively.

We may not be able to manage the growth of our business and our expansion plans and operations or implement our business strategies on schedule or within our budget, or at all.

Our business has become increasingly complex in terms of both the type and scale of our operations. Any expansion may increase the complexity of our operations and place a significant strain on our managerial, technological, operational, financial and human resources. We recently launched our online wholesale business and various value-added services, including online consultation services, cloud prescription services and data services. Our current and planned personnel, systems, procedures and controls may not be adequate to support our future operations. We cannot assure you that we will be able to effectively manage our growth or to implement all these systems, procedures and control measures successfully. If we are not able to manage our growth effectively, our business and prospects may be materially and adversely affected.

We are also continually executing a number of growth initiatives, strategies and operating plans designed to enhance our business, including launching various new services utilizing the latest big data and AI technologies. The anticipated benefits from these efforts

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are based on assumptions that may prove to be inaccurate. Moreover, we may not be able to successfully complete these growth initiatives, strategies and operating plans and realize all of the benefits that we expect to achieve or it may be more costly to do so than we anticipate. If, for any reason, the benefits we realize are less than our estimates or the implementation of these growth initiatives, strategies and operating plans adversely affect our operations or cost more or take longer to effectuate than we expect, or if our assumptions prove inaccurate, our business, financial condition and results of operations may be materially and adversely affected.

In addition, we may seek and pursue opportunities via joint ventures or strategic partnerships for expansion from time to time, and we may face similar risks and uncertainties as listed above. Failure to properly address these risks and uncertainties may materially and adversely affect our ability to carry out acquisitions and other expansion plans, integrate and consolidate newly acquired or newly formed businesses, and realize all or any of the anticipated benefits of such expansion, which may have a material adverse effect on our business, financial condition, results of operations and prospects.

We have incurred operating losses in the past, and may not be able to achieve or maintain profitability in the future.

We experienced net loss in the amount of RMB501.8 million, RMB467.1 million and RMB621.0 million (US\$97.5 million) in 2019, 2020 and 2021, respectively. We expect our operating costs and expenses to increase in the future in absolute terms as we expand our operations. We may also incur additional legal, accounting, and other expenses as a public company. If our revenue does not grow at a greater rate than our expenses, we will not be able to achieve and maintain profitability. We may incur significant losses in the future for various reasons, many of which may be beyond our control. Additionally, we may encounter unforeseen expenses, operating delays, or other unknown factors that may result in losses in the future. If our cost of sales and expenses continuously exceed our revenue, our business may be materially and adversely affected and we may not be able to achieve or maintain profitability.

Our pharmaceutical retail and wholesale businesses are subject to a variety of risks, which may have a material and adverse effect on our business, financial condition and results of operations.

We are subject to certain risks in our pharmaceutical retail and wholesale businesses, including:

- inability to successfully execute effective advertising, marketing and promotional programs necessary to maintain and increase awareness of our brands, products and services;
- failure to implement effective pricing and other strategies in response to market competition;
- inability to respond to changes in demand and preferences of pharmacy customers and consumers in a timely manner;
- inability to stock an adequate supply of pharmaceutical and other health and wellness products that meet the demand of our pharmacy customers and consumers;
- overall consumer spending on healthcare in China;
- inability to obtain and maintain regulatory or governmental permits, approvals and clearances, or to pass PRC government inspections or audits; and
- the risk of, and resulting liability from, any contamination, injury or other harm caused by any use, misuse or misdiagnosis involving products distributed by us.

The occurrence of any such risks in our pharmaceutical retail and wholesale businesses may damage our overall business and reputation, and may have a material and adverse effect on our financial condition and results of operations.

Our business generates and processes a large amount of data, and complying with evolving laws and regulations regarding cybersecurity, information security, privacy and data protection and other related laws and requirements may be expensive and may force us to make adverse changes to our business. Many of these laws and regulations are subject to changes and uncertain interpretations, and any failure to comply with these laws and regulations could result in negative publicity, legal proceedings, suspension or disruption of operations, increased cost of operations, or otherwise harm our business.

We generate and process a large amount of personal, transaction, demographic and behavioral data including medical records and other personal information. We face risks inherent in handling large volumes of data and in securing and protecting such data. In particular, we face a number of data-related challenges related to our business operations, including:

- protecting the data in and hosted on our system, including against attacks on our system by external parties or fraudulent behavior by our employees;
- addressing concerns related to privacy and sharing, safety, security and other factors; and
- complying with applicable laws, rules and regulations relating to the collection, storage, use, processing, transmission, provision, disclosure, deletion or security of personal information, including any requests from regulatory and government authorities relating to such data.

Regulatory requirements regarding the protection of such data are constantly evolving and can be subject to significant change, making the extent of our responsibility in that regard uncertain. Under certain regulations, rules and measures promulgated by the Ministry of Industry and Information Technology of the People’s Republic of China, or the MIIT, since 2011, any collection and use of a user’s personal information by an internet services provider must be subject to the consent of the user, abide by the principles of legality, rationality and necessity, and be within the specified purposes, methods and scopes. The internet services provider must keep all information collected strictly confidential and is prohibited from divulging, tampering with or destroying any such information, or selling or providing such information to other parties.

The PRC Cyber Security Law, which took effect in June 2017, created China’s first national-level data protection regime for “network operators,” which may include all organizations in China that provide services over the internet or other information network. Furthermore, in August 2018, the Standing Committee of China’s National People’s Congress, or the SCNPC promulgated the E-Commerce Law of the People’s Republic of China, or the E-Commerce Law, to regulate the e-commerce activities conducted within the territory of the PRC, which further strengthens the protection of consumers’ personal data and privacy. In addition, the PRC Data Security Law took effect in September 2021. Numerous regulations, guidelines and other measures have been or are expected to be adopted under the umbrella of, or in addition to, the Cyber Security Law and Data Security Law. For example, Regulations on the Security Protection of Critical Information Infrastructure, or the CII Protection Regulations, became effective in September 2021. According to the CII Protection Regulations, a critical information infrastructure operator, or a CIO, must take the responsibility to protect the CII’s security by performing certain prescribed obligations. For additional information, see “Item 4. Information on the Company—B. Business Overview—Regulations—Regulations relating to Internet Information Security and Privacy Protection.” As of the date of this annual report, we have not been identified as a CIO by the relevant regulatory authority.

The Personal Information Protection Law took effect in November 2021, integrates the various rules with respect to personal information rights and privacy protection. In December 2021, the Cyberspace Administration of China, or the CAC, and several other administrations jointly promulgated the amended Cybersecurity Review Measures, or the Cybersecurity Review Measures, which took effect in February 2022. Pursuant to the Cybersecurity Review Measures, if the relevant activity affects or may affect national security, a CIO that purchases network products and services or an internet platform operator that conducts data process activities shall be subject to the cybersecurity review. The Cybersecurity Review Measures also expands the cybersecurity review requirement to cover “internet platform operators” in possession of personal information of over one million users if such operators intend to list their securities in a foreign country. See “—Risks Related to Doing Business in China— The approval, filing or other requirements of the China Securities Regulatory Commission or other PRC government authorities may be required under PRC law in connection with our issuance of securities overseas.”

Furthermore, since September 2021, a series of laws and regulations relating to information security, privacy and data protection have been adopted. For more information, see “Item 4. Information on the Company—B. Business Overview—Regulations—Regulations relating to Internet Information Security and Privacy Protection.”

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Since these laws and regulations in China are relatively new, uncertainties still exist in relation to their interpretation and implementation. Any change in laws and regulations relating to privacy, data protection and information security and any enhanced governmental enforcement action of such laws and regulations could greatly increase our cost in providing our products and services, limit their use or adoption or require certain changes to be made to our operations. If we fail to comply with these new laws and regulations described above, we may be ordered to rectify and terminate any actions that are deemed illegal by the government authorities and become subject to fines and other government sanctions, which may materially and adversely affect our business, financial condition, and results of operations.

Our privacy policies and practices concerning the collection, storage, use, processing and disclosure of user data are posted on our mobile app. Any failure, or perceived failure, by us to comply with our privacy policies or with any applicable regulatory requirements or privacy protection-related laws, rules and regulations could result in proceedings or actions against us by governmental entities or others. These proceedings or actions may subject us to significant penalties and negative publicity, require us to change our business model or practices, increase our costs and severely disrupt our business, which may materially and adversely affect our business, financial condition, results of operations and prospects.

Our failure to properly manage various participants in our ecosystem may materially and adversely affect our business.

We rely on various participants, including, but not limited to, pharmacies, pharmaceutical companies, marketplace sellers and medical professionals, in the provision of services and products in our ecosystem, and the success of our business depends on our ability to properly manage them. See "Item 4. Information on the Company — B. Business Overview — Our Ecosystem."

We consider a variety of factors before entering into contractual arrangements with them. Nevertheless, we have limited control over the quality of work and performance of our ecosystem participants in their provision of services and products over our website and mobile platform or otherwise, and they may breach such contractual arrangements and subject us to claims and liabilities that may affect our business operations.

We have also implemented quality control standards and procedures to manage their work and performance in our ecosystem. However, there can be no assurance that our monitoring of their work and performance will be sufficient to ensure the quality of their work. In the event that a third party fails to meet our quality and operating standards contracted in our agreements or as required by relevant PRC laws and regulations, our operations may suffer and our business, financial condition and results of operations may be materially and adversely affected. Furthermore, because of the contractual relationships, we could be perceived as responsible for the actions of such participants and, as a result, suffer reputational damage. This may adversely affect our ability to attract new pharmacies, pharmaceutical companies, medical professionals and marketplace sellers, and to engage them as providers within our ecosystem.

Any lack of requisite approvals, licenses or permits applicable to our business, or any non-compliance with relevant laws and regulations, may have a material and adverse effect on our business, financial condition, results of operations and prospects.

Our business is subject to governmental supervision and regulation by various PRC governmental authorities including, but not limited to, the Ministry of Commerce of the People's Republic of China, or MOFCOM, the MIIT, the National Health and Family Planning Commission of the People's Republic of China, or the NHFPC, which was restructured and integrated into the National Health Commission of the People's Republic of China, or the NHC, National Medical Products Administration, formerly China Food and Drug Administration (the "NMPA" or "CFDA"), the State Administration for Market Regulation (the "SAMR"), formerly the State Administration for Industry and Commerce (the "SAIC"), the CAC, and the corresponding local regulatory authorities. Such government authorities promulgate and enforce laws and regulations that cover a variety of business activities that our operations concern, such as provision of internet information, online medical services, online and offline retail, sales and online operation of pharmaceutical products and medical devices, sales of food, and internet advertisement, among other things. These regulations in general regulate the entry into, the permitted scope of, as well as approvals, licenses and permits for, the relevant business activities.

In addition to obtaining necessary approvals, licenses and permits for conducting our business, we must comply with relevant laws and regulations. Our businesses, such as online and offline pharmaceutical retail and wholesale distribution and online healthcare services, are subject to various and complex laws and regulations, extensive government regulations and supervision. We may not be fully informed of all and new requirements under relevant laws and regulations in a timely manner, and even if we become aware of new requirements, due to uncertainties in their interpretations and implementation, it will be difficult for us to determine what actions or omissions would be deemed as violations of applicable laws and regulations. We may also not be able to respond to evolving laws

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and regulations and take appropriate action in time to adjust our business model. As a result, we may be in violation or non-compliance with such laws and regulations.

In particular, under the Administrative Measures for the Supervision and Administration of Circulation of Pharmaceuticals promulgated by the CFDA in 2007, a company is prohibited from selling prescription drugs to consumers without prescription, via internet or by post. A company in violation of such prohibitions will be instructed to rectify, given a disciplinary warning, and/or imposed an administrative penalty of no more than RMB30,000 per violation. See “Item 4. Information on the Company—B. Business Overview—Regulations—Regulations Relating to Online Operation of Drugs and Medical Devices.” The newly revised Drug Administration Law of the People’s Republic of China, or the Drug Administration Law, abolishes the restriction on online sale of prescription drugs and adopts the principle of keeping online and offline sales consistent, which allows the qualified pharmaceutical enterprise to conduct online sale of drugs (including prescription drugs, but not certain special controlled drugs). In addition, the entity that operates a third-party online drug transaction platform shall be filed with relevant authority for drugs supervision and administration and responsible to examine the qualifications of the drug marketing permit holders and drug operation enterprises applying to operate on its platform, ensure that they meet legal requirements, and manage the drug operation behaviors occurring on the platform. However, as of the date of this annual report, none of the regulations or implementation rules regulating online drug sales have yet been promulgated and implemented, which may further introduce and impose certain conditions and restrictions to the online sale of drugs. In the past, we had received disciplinary warnings and administrative penalties due to certain non-compliance incidents in relation to prescription drugs sales. We have adjusted our sales model and relevant functions of our online platforms in response to such warnings and penalties. However, it remains uncertain that our sales model and online platforms as adjusted are and will be in full compliance with the relevant laws and regulations, which are evolving and subject to changes. In addition, due to the complexity of our IT system, its potential errors, or human errors, mistakes or misconduct by our offline retail pharmacies, we cannot assure you that we can fully comply with and meet the requirements under all laws and regulations related to the sale of prescription drugs. Any failure to comply with such laws and regulations could materially and adversely affect our business, results of operations, financial condition and prospects.

Due to the uncertainties in the regulatory environment of the industries in which we operate, there can be no assurance that we have obtained or applied for all the approvals, permits and licenses required for conducting our business and all activities in the PRC, or that we would be able to maintain our existing approvals, permits and licenses or obtain any new approvals, permits and licenses if required by any future laws or regulations. If we fail to obtain and maintain approvals, licenses or permits required for our business, or to comply with relevant laws and regulations, we could be subject to liabilities, fines, penalties and operational disruptions, or we could be required to modify our business model, which could materially and adversely affect our business, financial condition and results of operations.

We may become subject to product liability and medical liability claims, which could cause us to incur significant expenses and be liable for significant damages if not covered by insurance.

We are exposed to risks inherent in marketing, distributing and selling pharmaceutical and other health and wellness products and providing online healthcare and medical services in China. Claims, customer complaints or administrative penalties may arise if any of the products we market and distribute are deemed or proven to be unsafe, ineffective or defective, or they are found to contain illicit substances. We may also be subject to allegations of having engaged in practices such as improper filling of prescriptions, distribution of counterfeit and substandard medicines, or providing inadequate warnings or insufficient or misleading disclosures of side effects.

In addition, in the event that any use or misuse of the products we distribute results in personal injury, suicide or death, product liability claims may be brought against us for damages. If we are unable to defend ourselves against such claims, among other things, we may be subject to civil liabilities for physical injury, death or other losses caused by our products, to criminal liabilities, and to the revocation of our business licenses. In addition, we may be required to suspend sales or cease sales of the relevant products.

We face risks of medical liability claims against our in-house medical team, external doctors and us. We only carry insurance covering medical malpractice claims for our in-house doctors and some of our external doctors. Adequate professional malpractice insurance coverage may not be available to our in-house medical team, external doctors or us in the future on commercially acceptable terms, or at all.

Any claims made against us that are not fully covered by insurance could be costly to defend against, result in substantial damage awards against us and divert the attention of our management and our in-house medical team and external doctors from our operations, which could have a material adverse effect on our business, financial condition, results of operations and reputation.

If we are unable to implement our strategy to expand our PRC operations by completing an initial public offering and listing on the STAR Market, our ability to strengthen our market position and operations in the PRC could be materially impaired. If our redemption obligation is triggered by a failure to complete the STAR Market listing, we may not have available liquidity to meet investor redemptions. Even if we complete the STAR Market listing, we may not achieve the results contemplated by our business strategy and our strategy for growth in the PRC may not result in increase in the trading price of our ADSs.

In August 2020 we announced plans to seek to list the shares of 1 Pharmacy Technology (Shanghai) Co., Ltd. (previously known as Yao Fang Information Technology (Shanghai) Co., Ltd. and 1 Pharmacy Yao Fang Technology (Shanghai) Co., Ltd.), or 1 Pharmacy Technology, on the Science and Technology Innovation Board of Shanghai Stock Exchange (the “STAR Market”) within the next three years (the “STAR Listing”). 1 Pharmacy Technology is our principal operating company and was a wholly owned subsidiary of Yao Wang Corporation Limited, or Yao Wang. See “Item 4. Information on the Company — A. History and Development of the Company.” Since August 20, 2020, 1 Pharmacy Technology has become a majority owned subsidiary of Yao Wang. We may not be able to complete the STAR Listing for a number of reasons, many of which are outside our control. 1 Pharmacy Technology must succeed in obtaining PRC governmental approvals required to permit the STAR Listing, and one or more of those approvals may be denied, or significantly delayed, by the PRC regulators for reasons outside our control or unknown to us. Similarly, the STAR Listing application may be denied or delayed by the Shanghai Stock Exchange and/or China Securities Regulatory Commission in its discretion.

If we are unable to complete the STAR Listing, we may not otherwise be able to realize the advantages to our PRC operations contemplated by our business strategy, including accessing a new source of growth capital, raising our profile with Chinese investors and potential customers, and strengthening our leading digital healthcare platform in China. Because it may be more than three years before we know whether the STAR Listing will be completed, we may, in the interim, forego or postpone other alternative actions to strengthen our market position and operations in the PRC.

We cannot assure you that, even if the STAR Listing is completed, we will realize any or all of our anticipated benefits of the STAR Listing. Our completion of the STAR Listing may not have the anticipated effects of including the strengthening of our market position and operations in the PRC. If the STAR Listing is completed, 1 Pharmacy Technology will have broad discretion in the use of the proceeds from the initial sales of shares to investors and the proceeds from the initial public offering, and it may not spend or invest those proceeds in a manner that results in our operating success or with which our stockholders agree. Our failure to successfully leverage the completion of the STAR Listing to expand our PRC business could result in a decrease in the trading price of the ADSs, and we cannot assure you that the success of 1 Pharmacy Technology will have an attendant positive effect on the trading price of our ADSs.

Additionally, in the event that 1 Pharmacy Technology’s proposed listing on the STAR Market is not completed before June 30, 2023 (or the date otherwise agreed by 1 Pharmacy Technology and the investors in writing), such investors may choose to exercise their options to require the controlling shareholder of 1 Pharmacy Technology, Yao Wang, to redeem all or part of the equity interests then owned by such investors. As of December 31, 2021, we recorded redeemable non-controlling interests of RMB1,000,849. If the investors were to exercise such option, Yao Wang may not have sufficient fund for the redemption, and to the extent Yao Wang requires additional funding, we cannot assure you that such capital will be available on terms acceptable to us, or at all. Any such lack of fund may cause our defaults under the agreements between us and the investors and may impair our reputation and ability to grow its operations, which could have a material adverse effect on our operating results and on the price of the ADSs.

Failure to maintain optimal inventory levels and assortment of products could increase our operating costs or lead to unfulfilled customer orders, either of which could have a material and adverse effect on our business, financial condition, results of operations and prospects.

We need to maintain optimal inventory levels in order to operate our pharmaceutical retail and wholesale businesses successfully and to meet the demands of pharmacy customers and consumers. We manage inventories of pharmaceutical and other health and wellness products under our direct sales model, while marketplace sellers manage inventories of their products. We are exposed to inventory risk as a result of rapid changes in product life cycles, changing consumer preferences, uncertainty of product developments and launches, manufacturer back orders and other vendor-related problems, as well as the volatile economic environment in China. We cannot assure you that we will accurately predict these trends and events and avoid over-stocking or under-stocking of products. Furthermore, demand for products could change significantly between the time when the products are ordered and the time when they are ready for delivery. When we begin to sell a new product, it is particularly difficult to forecast product demand accurately.

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As our pharmaceutical retail and wholesale businesses carry a wide range of products and maintain significant inventory levels for a substantial portion of our merchandise, we may be unable to sell such inventory in sufficient quantities or during the relevant sales seasons. We had net write-downs of our inventories to their net realizable value of RMB790 thousand, RMB24.2 million and RMB46.0 million (US\$7.2 million) in 2019, 2020 and 2021, respectively. Inventory levels in excess of customer demand may result in inventory write-downs, expiration of products or an increase in inventory holding costs and a potential negative effect on our liquidity.

Conversely, if we underestimate customer demand, or if our suppliers fail to provide products to us in a timely manner, we may experience inventory shortages, which may, in turn, result in unfulfilled customer orders, leading to a negative impact on our customer relationships. We cannot assure you that we will be able to maintain proper inventory levels for our pharmaceutical retail and wholesale operations, and any such failure may have a material and adverse effect on our business, financial condition, results of operations and prospects.

We closely monitor the inventory levels of other products of which our marketplace sellers manage inventories. However, there can be no assurance that our monitoring and related measures will be effective in ensuring fulfillment of our customers' orders at our online retail pharmacy and online wholesale pharmacy. Our failure to maintain proper inventory levels for our retail and wholesale businesses may have a material and adverse effect on our business, financial condition, results of operations and prospects.

Third-party logistics and delivery companies are used to fulfill and deliver orders placed on our platform. If these logistics and delivery companies fail to provide reliable delivery services, our business and prospects, as well as our financial condition and results of operations, may be materially and adversely affected.

We leverage our large-scale operations and reputation to enter into contractual arrangements with a number of third-party delivery companies to deliver our products to our pharmacy customers and consumers. We may also use third-party service providers to ship products from our fulfillment centers to delivery stations or to deliver bulky item products. Interruptions to or failures in these third parties' delivery services could prevent the timely or proper delivery of our products to pharmacy customers and consumers. These interruptions may be due to events that are beyond our control or the control of these delivery companies, such as inclement weather, natural disasters, transportation disruptions or labor unrest. We may not be able to find alternative delivery companies to provide delivery services in a timely and reliable manner, or at all. If products are not delivered in proper condition or on a timely basis, our business and reputation could suffer.

Our self-developed technologies are complex and may contain undetected errors or may not operate properly, which could adversely affect our business, financial condition and results of operations.

Our self-developed technology platform provides our consumers and other participants in our ecosystem with the ability to conduct a variety of actions essential to the operations of our business and the delivery of our solution. Technology development is time-consuming, expensive and complex, and may involve unforeseen difficulties. We may encounter technical obstacles, and it is possible that we may discover additional problems that prevent our technologies from operating properly and consequently adversely affect our information infrastructure and other aspects of our business where our technologies are applied. If our solution does not function reliably in terms of performance, we may lose existing, or fail to attract new participants to our platform, which may damage our reputation and adversely affect our business.

Moreover, data services, supply chain management systems, and other proprietary technologies we provide to pharmacies, pharmaceutical companies and other customers are complex and those we offer may develop or contain undetected defects or errors. Material performance problems, defects or errors in our existing or new software and applications and services may arise in the future and may result from interface issues between our systems and data that we did not develop and the function of which is beyond our control or undetected in our testing. These defects and errors, and any failure by us to identify and address them, could result in loss of revenue or market share, diversion of development resources, harm to our reputation and increased service and maintenance costs. Defects or errors may discourage existing or potential customers from utilizing our solution. Correction of defects or errors could prove to be impossible or impracticable. The costs incurred in correcting any defects or errors may be substantial and could have a material adverse effect on our business, financial condition and results of operations. Defects or errors may also affect our pharmacies, pharmaceutical companies or other customers who rely on our self-developed technologies in the operation of their businesses, which may have a material adverse effect on our reputation, business, results of operations and prospects.

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We may be subject to penalties or disputes against us for failure to manage the multi-institution practices of our in-house medical team and external doctors.

The practice of doctors is strictly regulated under PRC laws, rules and regulations. Doctors who practice at medical institutions must hold practicing licenses and may only practice within the scope of their licenses and at the specific medical institutions as stated in their licenses. A doctor is required to register the medical institutions at which he or she practices in his or her license. If a doctor is found practicing at a medical institution not registered in his or her license, the doctor would be subject to regulatory penalties, from warning to suspension of practice and, in the worst-case scenario, revocation of licenses. A doctor practicing in multiple institutions must apply to register or file with competent in-charge administrative authorities and can only have the right to prescribe medicine at the registered or filed practicing institution. If the doctor issues a prescription in a medical institution not registered in his or her license, the relevant medical institution would also be subject to regulatory penalties, including a fine of up to RMB5,000 and, in the worst-case scenario, revocation of the medical institution's Practicing License for Medical Institutions.

We cannot assure you that our in-house and external doctors will complete the registration and relevant government procedures in a timely manner, or at all, or that our in-house and external doctors will not practice outside the permitted scope of their respective licenses. Our failure to properly manage the registration of our in-house doctors may subject us to administrative penalties against our medical institution, including fines, or, in the worst-case scenario, revocation of our Practicing License for Medical Institutions, any of which could materially and adversely affect our business. Meanwhile, if our in-house and external doctors are found to have deficient registration or found to be practicing beyond the scope permitted by relevant authorities, they may be disciplined and lose their practicing licenses. In the event that the multi-institution practices of our in-house and external doctors are in breach of their contractual obligations owed to other institutions, such as non-compete obligations, we may be exposed to indemnity or other legal liabilities if we are deemed to have aided in these breaches, and are therefore susceptible to legal disputes and potential damages. As a result, we may no longer be able to employ them in offering our online consultation services, which could materially and adversely affect our business. In addition, there can be no assurance that we could timely find qualified replacements on commercially reasonable terms, or at all.

We may not be able to prevent others from unauthorized use of our intellectual property, which could harm our business and competitive position.

We regard our trademarks, copyrights, patents, domain names, know-how, proprietary technologies, and similar intellectual property as critical to our success, and we rely on a combination of intellectual property laws and contractual arrangements, including confidentiality agreements with our employees and third parties, to protect our proprietary rights. Despite these measures, it is often difficult to enforce intellectual property rights in China. Even where adequate laws exist, certain procedural issues create effective obstacles to the proper enforcement of intellectual property rights. In addition, the available remedies in both court proceeding and through administrative enforcement are often inadequate to address infringement or to provide intellectual property rights holders with full compensation for the losses caused. Accordingly, we may not be able to effectively protect our intellectual property rights or to enforce confidentiality undertakings in China. In addition any of our intellectual property rights could be challenged, invalidated, circumvented or misappropriated, or such intellectual property may not be sufficient to provide us with competitive advantages. In addition, although we are not aware of any copycat websites or mobile apps that attempt to cause confusion or traffic diversion from us at the moment, we may become an attractive target to such attacks in the future because of our brand recognition.

In addition, there can be no assurance that our patent applications would be approved, that any issued patents would adequately protect our intellectual property, or that such patents would not be challenged by third parties or found by a judicial authority to be invalid or unenforceable.

We may be subject to allegations, lawsuits and administrative penalties relating to the sale, distribution, marketing and advertising of counterfeit or substandard products in our pharmaceutical retail and wholesale businesses, which may damage our brand and reputation and have a material adverse effect on our business, financial condition, results of operations and business prospects.

Certain products distributed or sold in the pharmaceutical retail and wholesale markets in China may be manufactured without proper licenses or approvals and/or fraudulently mislabeled with respect to their content and/or manufacturer. These products are generally referred to as counterfeit or substandard pharmaceutical products. The current counterfeit and substandard product regulation control and enforcement system in China is not sufficiently mature to completely eliminate the manufacturing and sales of counterfeit pharmaceutical products. Counterfeit and substandard pharmaceutical products are generally sold at lower prices than authentic pharmaceutical products, and, in some cases, are very similar in appearance to the authentic pharmaceutical products.

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Therefore, the presence of counterfeit products of pharmaceuticals distributed or sold by us can quickly erode our sales volumes and revenue for the relevant products.

Furthermore, counterfeit or substandard products may or may not have the same chemical composition as the authentic counterparts, which may make them less effective than the authentic ones, entirely ineffective, or more likely to cause severe adverse side effects. We may not be able to identify those counterfeit or substandard products we source from our suppliers. Any unintentional and unknowing sales of counterfeit or substandard products in our pharmaceutical distribution or retail businesses, or sales of counterfeit and substandard products by third parties illegally using our brand names, may subject us to negative publicity, fines and other administrative penalties, or even result in litigation relating to the sale, marketing and advertising of those products. Moreover, the continuing presence of counterfeit and substandard products may reinforce the negative image of distributors and retail pharmacies among consumers in general, and may severely harm the reputation and brand names of pharmaceutical companies, including ourselves. Similarly, consumers may buy counterfeit and substandard products that are in direct competition with products distributed or sold in our pharmaceutical retail and wholesale businesses, which may materially and adversely affect the sales volumes of the relevant products in our portfolio and further impact our business, financial condition, results of operations and prospects.

If we fail to provide satisfactory customer experience and continue to increase our retail and wholesale customer base, our business may be materially and adversely affected.

Our business is highly dependent on the receptiveness of our pharmacy customers and consumers to our services and products as well as their willingness to use, and to increase the frequency and extent of their utilization of, our solution. Their degree of receptiveness to our services and products depends on a number of factors, including the demonstrated accuracy and efficacy of our offerings compared to those of others, turnaround time, cost-effectiveness, convenience and marketing support. In addition, negative publicity concerning our solution or the internet healthcare market as a whole could limit market acceptance of our solution, especially that of the online consultation services. Meanwhile, there can be no assurance that our efforts and ability to demonstrate the value of our solution and the relative benefits of our services and products over those of our competitors to our pharmacy customers and consumers would be successful. If we fail to achieve an adequate level of acceptance by our pharmacy customers and consumers of our services and products, or if our solution does not drive their engagement, then our business may not develop as expected, or at all, and our business, financial condition or results of operations may be materially and adversely affected.

The success of our business also hinges on our ability to provide satisfactory customer experience, which depends on our ability to continue to deliver quality care to our users, to maintain the quality of our services and products, to source services and products that are responsive to customer demands, and to provide timely and reliable delivery, flexible payment options and satisfactory after-sales services. Such ability, in turn, depends on a variety of factors beyond our control. In particular, we rely on a number of third parties in the provision of our services and products. Their failure to provide a high-quality customer experience to our pharmacy customers and consumers may adversely affect our pharmacy customers' and consumers' receptiveness of, and willingness to utilize our solution, which may damage our reputation and cause us to lose pharmacy customers and consumers.

In addition, we operate a customer service center to provide assistance to our pharmacy customers and consumers. If our customer service representatives fail to provide satisfactory service, or if waiting times are too long due to high volume of inquiries from customers at peak times, our brand and customer loyalty may be adversely affected. Moreover, any negative publicity or poor feedback on our customer service may harm our brand and reputation and, in turn, cause us to lose pharmacy customers and consumers and market share.

The failure of in-house medical team and external doctors to provide adequate and proper service to consumers may have a material and adverse effect on our business, financial condition and results of operations.

Our in-house medical team, external doctors and other employees, may provide sub-standard services, mishandle sensitive information, engage in other misconduct or commit medical malpractice, which could subject us to medical liability claims. Our business, financial condition, results of operations and reputation may be materially and adversely affected if any such claims are made against us in connection with these actions that are not fully covered by insurance. See “—We may become subject to product liability and medical liability claims, which could cause us to incur significant expenses and be liable for significant damages if not covered by insurance.” With respect to external doctors, as they often work remotely, we have limited control over them as well as the quality of their online medical consultation services. There can be no assurance that our risk management procedures will be sufficient to monitor their performance and control the quality of their work. In the event that the external doctors fail to comply with the contractual obligations and applicable laws in relation to the provision of our online consultation services, our user experience could

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deteriorate, and we may suffer as a result of any actual or alleged misconduct by them, which could materially and adversely affect our business, financial condition, results of operations and reputation.

The failure of our marketplace sellers to control the quality of products they sell on our platform, or to make timely and accurate delivery of their products sold on our platform, may have a material and adverse effect on our business, financial condition and results of operations.

Under the direct sales model, we manage inventories in an integrated process. Under our marketplace model, many of our marketplace sellers use their own facilities to store their products and utilize their own or third-party delivery systems to deliver their products to our pharmacy customers and consumers, which makes it difficult for us to ensure that our pharmacy customers and consumers get consistent quality products and services for all products sold through our online platforms. If any marketplace seller fails to control the quality of the products that it sells on our platforms, or if it does not deliver the products or delivers them late or delivers products that are materially different from their description, or if it sells counterfeit or unlicensed products through our platforms, or if it does not possess requisite licenses or permits as required by relevant laws and regulations despite our online background check for such licenses or permits on the marketplace seller, the reputation of our retail and wholesale pharmacy and our brand may be materially and adversely affected and we could face claims and may be held liable for damages in connection with such claims.

Any disruption to the operation of our current fulfillment facilities, or to the development of our new facilities, could reduce or negatively impact sales and have a material adverse effect on our business, financial condition and results of operations.

We rely on our fulfillment centers for the continuing operation of our pharmaceutical distribution business. Natural disasters or other unanticipated catastrophic events, including power interruptions, water shortage, storms, fires, earthquakes, terrorist attacks and wars, as well as changes in governmental planning for the land underlying these facilities, could significantly impair our ability to operate our business and destroy any inventory located in these facilities. In addition, our fulfillment centers that meet the requirements of modern logistics operations for guaranteed storage safety, optimal and flexible space utilization and high operational efficiency are in short supply. We may not be able to replace these facilities and equipment in a timely manner, should any of the foregoing occur.

Furthermore, the leases for our fulfillment centers and our use thereof could be challenged by third parties or government authorities, which may cause interruptions to our business operations. Certain lessors of our leased fulfillment centers have not provided us with their property ownership certificates or any other documentation proving their right to lease those properties to us. If our lessors are not the owners of the properties and they have not obtained consents from the owners or their lessors or permits from the relevant government authorities, our leases could be invalidated and we may have to renegotiate the leases with the owners or the parties who have the right to lease the properties, and the terms of the new leases may be less favorable to us. Also, certain of our leasehold interests in leased properties have not been registered with the relevant PRC government authorities as required by PRC law, which may expose us to potential fines. Although we are not aware of any claims or actions being contemplated or initiated by government authorities, property owners or any other third parties with respect to our leasehold interests in or use of such properties, we cannot assure you that our use of such leased properties will not be challenged. In the event that our use of leased properties is successfully challenged, we may be subject to fines and forced to relocate the affected operations. We can provide no assurance that we will be able to find suitable replacement sites on terms acceptable to us on a timely basis, or at all, or that we will not be subject to material liability resulting from third parties' challenges on our use of such properties.

Our wide variety of accepted payment methods subjects us to third-party payment processing-related risks.

We accept payments using a variety of methods, including payment on delivery, bank transfers, online payments with credit cards and debit cards issued by major banks in China, and payment through third-party online payment platforms. For certain payment methods, including credit and debit cards, we pay interchange and other fees, which may increase over time and raise our operating costs and lower our profit margins. We may also be subject to fraud and other illegal activities in connection with the various payment methods we offer, including online payment and cash-on-delivery options. We also rely on third parties to provide payment processing services. We use third-party couriers to deliver all of the orders. The delivery personnel of our third-party couriers collect payments on our behalf if our customers opt for the payment-on-delivery option, and we require the third-party couriers to remit the payment collected to us on the following day. If these companies fail to remit the payment collected to us in a timely fashion, or at all, if they become unwilling or unable to provide these services to us, or if their service quality deteriorates, our business could be disrupted. We may also be subject to fraud and other illegal activities in connection with the various payment methods we offer, including online payment and cash-on-delivery options. Although we rely on third parties to provide payment processing services, we are also subject to various rules, regulations and requirements, regulatory or otherwise, governing electronic funds transfers, which could change or be reinterpreted to make it difficult or impossible for us to comply. If we fail to comply with these rules or requirements, we may be subject to fines and higher transaction fees and lose our ability to accept credit and debit card payments from our pharmacy customers and consumers, process electronic funds transfers or facilitate other types of online payments, and our business, financial condition and results of operations could be materially and adversely affected.

Any damage to the reputation and recognition of our brand names, including negative publicity against us, may materially and adversely affect our business operations and prospects.

We depend on our reputation and brand names in many aspects of our business operations. However, we cannot assure you that we will be able to maintain a positive reputation or brand name for all of our products in the future. Our reputation and brand names may be materially and adversely affected by a number of factors, many of which are beyond our control, including:

- adverse associations with the third party-branded products we sell or which are sold in our stores or on our platform, including with respect to their efficacy or side effects;
- lawsuits and regulatory investigations against us or otherwise relating to our products or industry;
- improper or illegal conduct by our employees, retail and wholesale pharmacies and third-party promoters, that is not authorized by us; and
- adverse publicity associated with us, our products or our industry, whether founded or unfounded.

Any damage to our brand names or reputation as a result of these or other factors may cause our products to be perceived unfavorably by pharmacies, doctors, regulators and consumers and the existing and prospective employees, retail and wholesale pharmacies and third-party promoters, and our business operations and prospects could be materially and adversely affected as a result.

Our business may be materially and adversely affected by adverse news, scandals or other incidents associated with the PRC general health and wellness industry.

Incidents that reflect doubt as to the quality or safety of pharmaceutical products manufactured, distributed or sold by other participants in the PRC general health and wellness industry, particularly the internet healthcare industry, including our competitors, have been, and may continue to be, subject to widespread media attention. Such incidents may damage the reputation of not only the parties involved, but also the general health and wellness industry in general, even if such parties or incidents have no relation to us, our management, our employees, our suppliers, our distributors or our retail pharmacies. Such negative publicity may indirectly and adversely affect our reputation and business operations. In addition, incidents not related to product quality or safety, or other negative publicity or scandals implicating us or our employees, regardless of merit, may also have an adverse impact on us and our reputation and corporate image.

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If our risk management and internal control system is not adequate or effective, and if it fails to detect potential risks in our business as intended, our business, financial condition and results of operations could be materially and adversely affected.

We have established our internal control system, such as an organizational framework and, policies and procedures that are designed to monitor and control potential risk areas relevant to our business operations. However, due to the inherent limitations in the design and implementation of our internal control system, our internal control system may not be sufficiently effective in identifying, managing and preventing all risks if external circumstances change substantially or extraordinary events take place.

Furthermore, our new business initiatives may give rise to additional internal control risks that are currently unknown to us, despite our efforts to anticipate such issues. If our internal control system fails to detect potential risks in our business as intended or is otherwise exposed to weaknesses and deficiencies, our business, financial condition and results of operations could be materially and adversely affected.

Our risk management and internal controls also depend on effective implementation by our employees. There can be no assurance that such implementation by our employees will always function as intended or such implementation will not involve any human errors, mistakes or intentional misconduct. If we fail to implement our policies and procedures in a timely manner, or fail to identify risks that affect our business with sufficient time to plan for contingencies for such events, our business, financial condition and results of operations could be materially and adversely affected, particularly with respect to the maintenance of our relevant approvals and licenses granted by governments.

We may experience failures in our information technology system, which could materially and adversely affect our business, financial condition and results of operations.

We depend heavily on our information technology system to manage our business processes, to record and process our operational and financial data, and to provide reliable services. We have built secure, stable and scalable IT infrastructure. However, our information technology system may fail due to natural disasters or failures of public infrastructure, our information technology infrastructure or our applications software systems that are wholly or partially beyond our control. Any material disruption to the operation of our information technology system could have a material adverse effect on our business. Our failure to address these problems could result in our inability to perform, or delays in our performance of, critical business operational functions, loss of key business data, or our failure to comply with regulatory functions, which could materially and adversely affect our business operations and customer service.

We may be held liable for information or content displayed on, retrieved from or linked to our mobile applications or website, which may materially and adversely affect our business and operating results.

In addition to our website, we also offer healthcare products and services through our mobile applications, which are regulated by the Administrative Provisions on Mobile Internet Applications Information Services, or the APP Provisions, promulgated by the CAC, on June 28, 2016 and effective on August 1, 2016. According to the APP Provisions, the providers of mobile applications shall not create, copy, publish or distribute information and content that is prohibited by laws and regulations. We have implemented internal control procedures screening the information and content on our mobile applications to ensure their compliance with the APP Provisions. However, we cannot assure that all the information or content displayed on, retrieved from or linked to our mobile applications complies with the requirements of the APP Provisions and other related regulations and rules at all times. If our mobile applications were found to be violating the APP Provisions, we may be subject to administrative penalties, including warning, service suspension or removal of our mobile applications from the relevant mobile application store, which may materially and adversely affect our business and operating results.

We rely on assumptions and estimates to calculate certain key operating metrics, and inaccuracies in such metrics may harm our reputation and adversely affect our business.

Certain key operating metrics in this annual report are calculated using our internal data that have not been independently verified by third parties. While these numbers are based on what we believe to be reasonable calculations for the applicable periods of measurement, there are some challenges in measuring those metrics, such as GMV and repurchase rate. In addition, our key operating metrics are derived and calculated based on different assumptions and estimates, and you should be cautious of such assumptions and estimates when assessing our operating performance.

Our operating metrics may differ from estimates published by third parties or from similarly titled metrics used by our competitors due to differences in data availability, sources and methodology. If third parties do not perceive our user metrics to be accurate representations of our user base or user engagement, or if we discover material inaccuracies in our operating metrics, our reputation may be harmed and third parties may be less willing to allocate their resources or spending to us, which could adversely affect our business and operating results.

Some pharmaceutical products offered by us are subject to price restrictions and will continue to be subject to price competition in China, but may be pending on changes of the regulations.

Some of our pharmaceutical products were subject to government price controls in the form of fixed retail prices or retail price ceilings and periodic downward adjustments imposed by National Development and Reform Commission, or the NDRC, and other authorities. Pursuant to the Notice Regarding the Opinion on Facilitating the Pharmaceutical Pricing Reform jointly issued by the National Development and Reform Commission, or the NDRC, the NHFPC and five other PRC government agencies in May 2015, the price ceilings imposed by the PRC government on pharmaceutical products other than narcotic and Class I psychotropic drugs were lifted on June 1, 2015, and these products would be subject to a more market-based pricing system adopted by medical insurance bureaus and relevant authorities.

Even prior to the lifting of government price controls on pharmaceutical products, the prices of prescription drugs in China had been determined by the centralized tender process and the prices of OTC drugs in China had been determined by arm's-length, commercial negotiation and market factors such as brand recognition, market competition and consumer demand. There is no assurance that the application of the more market-based pricing system will result in a higher product pricing compared to the government-controlled pricing, as competition from other retailers and wholesalers, particularly those offering the same products but with lower prices, may force us to lower our sales prices to the previous government-controlled price levels. Consequently, our profitability may suffer and our business, financial condition and results of operations may also be materially and adversely affected.

In addition, since 2019, the State Council and other relevant authorities have issued a series of policies on deepening the reform of medical and healthcare system which is intended to organize centralized procurement, lower drug price, reduce the burden on patients of drug costs, and lower the transaction costs of pharmaceutical enterprises. The Guidance on Improving "Internet +" Medical Service Price and Medical Insurance Payment Policies issued by the National Healthcare Security Administration, or the NHSA, proposed to improve project management, optimize the pricing mechanism and clarify the payment policy of "Internet +" medical services. Although such policies may lower the transaction costs of the pharmaceutical enterprises and increase the amount of drugs purchased, they may also reduce the sales prices of the drugs and increase market competition within the pharmaceutical industry. While there are still uncertainties relating to the actual implementation of such policies, the downward pressure brought by government policies on drug prices may adversely affect our business, financial condition and results of operations.

If any failure to implement and maintain an effective system of internal controls results in a material weakness over financial reporting, we may be unable to accurately report our results of operations, meet our reporting obligations or prevent fraud, and investor confidence and the trading price of the ADSs may be materially and adversely affected.

We are subject to reporting obligations under the U.S. securities laws. The SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring every public company to include a management report on the company's internal control over financial reporting in its annual report, which contains management's assessment of the effectiveness of our internal control over financial reporting. Our management has concluded that our internal control over financial reporting was effective as of December 31, 2021. See "Item 15. Controls and Procedures—Management's Annual Report on Internal Control over Financial Reporting." Our independent registered public accounting firm has issued an attestation report, which has concluded that our internal control over financial reporting is effective as of December 31, 2021.

However, any failure to achieve and maintain effective internal control over financial reporting could result in the loss of investor confidence in the reliability of our consolidated financial statements, which in turn could harm our business and negatively impact the trading price of the ADSs. Furthermore, we have incurred and anticipate that we will continue to incur considerable costs, management time and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes-Oxley Act. 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 the Nasdaq, regulatory investigations and civil or criminal sanctions.

Competition for employees is intense, and we may not be able to attract and retain the qualified and skilled employees needed to support our business.

We believe our success depends on the efforts and talent of our employees, including medical professionals, risk management, software engineering, financial and marketing personnel. Our future success depends on our continued ability to attract, develop, motivate and retain qualified and skilled employees. Competition for highly skilled technical, risk management and financial personnel is extremely intense. We may not be able to hire and retain these personnel at compensation levels consistent with our existing compensation and salary structure. Some of the companies with which we compete for experienced employees have greater resources than we have and may be able to offer more attractive terms of employment.

In addition, we invest significant time and expenses in training our employees, which increases their value to competitors who may seek to recruit them. If we fail to retain our employees, we could incur significant expenses in hiring and training new employees, and the quality of our services and our ability to serve various participants in the pharmaceutical value chain could decline, resulting in a material adverse effect to our business.

Our business depends on the continued efforts of our senior management. If one or more of our key executives were unable or unwilling to continue in their present positions, our business may be severely disrupted.

Our future success depends heavily upon the continued services of our senior executives, key research and development personnel and key sales and marketing personnel. We rely on the expertise and experience of our founders, Dr. Gang Yu and Mr. Junling Liu, especially in areas of supply chain management and e-commerce. Our research and development team is critical to the development of proprietary technologies used by our online and offline, retail and wholesale businesses, and realization of the potential benefits of our intellectual property. In addition, success in the distribution of our products depends on the dedication and skills of our sales and marketing personnel. Accordingly, our ability to attract and retain key personnel is a critical factor in our competitiveness. Competition for these individuals could require us to offer higher compensation and other benefits in order to attract and retain them, which could increase our operating expenses and, in turn, materially and adversely affect our financial condition and results of operations. If we are unable to attract or retain the personnel required to achieve our business objectives, our business could be severely disrupted.

We do not maintain key-person insurance for members of our management team. If we lose the services of any senior management, we may not be able to identify suitable or qualified replacements, and may incur additional expenses to recruit and train new personnel, which could severely disrupt our business and prospects and prolong our expansion strategies and plans. Furthermore, if any of our executive officers joins a competitor or forms a competing company, we may lose a significant number of our existing pharmacy customers and consumers and potentially lose our substantial research and development achievements, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

We may from time to time become party to litigation, other legal or administrative disputes and proceedings that may materially and adversely affect us.

In the course of our ordinary business operations, we may become a party to litigation, legal proceedings, claims, disputes or arbitration proceedings from time to time. Any ongoing litigation, legal proceedings, claims, disputes or arbitration proceedings may distract our senior management's attention and consume our time and other resources. In addition, even if we ultimately succeed in such litigation, legal proceedings, claims, disputes or arbitration proceedings, there may be negative publicity attached to such litigation, legal proceedings, claims, disputes or arbitration proceedings, which may materially and adversely affect our reputation and brand names. In the case of an adverse verdict, we may be required to pay significant monetary damages, assume significant liabilities or suspend or terminate parts of our operations. As a result, our business, financial condition, results of operations and prospects may be materially and adversely affected.

We may not have sufficient insurance to cover our business risks.

We have obtained insurance to cover certain potential risks and liabilities, such as professional liability insurance for our doctors in connection with their provision of medical consultation services over our platform, and product liability insurance for us and our suppliers with respect to products sold in our retail pharmacy and online wholesale pharmacy through 1 Medicine Marketplace and 1 Pharmacy, respectively. However, we may not be able to acquire any insurance for certain types of risks such as business liability or service disruption insurance for all of our operations in the PRC, and our coverage may not be adequate to compensate for all losses that may occur, particularly with respect to loss of business or operations. For example, we do not maintain business interruption insurance, nor do we maintain key-man life insurance. Any business disruption, litigation, regulatory action, outbreak of epidemic disease or natural disaster could also expose us to substantial costs and diversion of resources. There can be no assurance that our insurance coverage is sufficient to prevent us from any loss or that we will be able to successfully claim our losses under our current insurance policies on a timely basis, or at all. If we incur any loss that is not covered by our insurance policies, or the compensated amount is significantly less than our actual loss, our business, financial condition and results of operations could be materially and adversely affected.

We may be subject to intellectual property infringement claims, which may be expensive to defend and may disrupt our business and operations.

We cannot be certain that our operations or any aspects of our business do not or would not infringe upon or otherwise violate trademarks, patents, copyrights or other intellectual property rights held by third parties. We may be, from time to time, or in the future, become subject to legal proceedings and claims relating to the intellectual property rights of others. In addition, there may be other third-party intellectual property that is infringed by our products, services or other aspects of our business. There could also be existing intellectual property of which we are not aware that our products may inadvertently infringe. There can be no assurance that holders of such intellectual property purportedly relating to some aspect of our technology platform or business, if any such holders exist, would not seek to enforce such intellectual property against us in the PRC or in any other jurisdictions, as applicable. Furthermore, the application and interpretation of PRC intellectual property related laws and the procedures and standards in the PRC are still evolving and are uncertain, and there can be no assurance that PRC courts or regulatory authorities would agree with our analysis. If we are found to have violated the intellectual property rights of others, we may be subject to liability for our infringement activities or may be prohibited from using such intellectual property, and we may incur licensing fees or be forced to develop alternatives of our own. In addition, we may incur significant expenses, and may be forced to divert management's time and other resources from our business and operations to defend against these third-party infringement claims, regardless of their merits. Successful infringement or licensing claims made against us may result in significant monetary liabilities and may materially disrupt our business and operations by restricting or prohibiting our use of the intellectual property in question, which may materially and adversely affect our business, financial condition and results of operations.

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Failure to renew our current leases or locate desirable alternatives for our facilities could materially and adversely affect our business.

We lease properties for our offices, offline retail pharmacies and fulfillment centers. We may not be able to successfully extend or renew such leases upon expiration of the current term on commercially reasonable terms or at all, and may therefore be forced to relocate our affected operations. This could disrupt our operations and result in significant relocation expenses, which could adversely affect our business, financial condition and results of operations. In addition, we compete with other businesses for premises at certain locations or of desirable sizes. As a result, even though we could extend or renew our leases, rental payments may significantly increase as a result of the high demand for the leased properties. In addition, we may not be able to locate desirable alternative sites for our facilities as our business continues to grow and failure in relocating our affected operations could adversely affect our business and operations.

Security breaches and attacks against our systems and network, and any potential resultant breach or failure to otherwise protect confidential and proprietary information, could damage our reputation and adversely affect our business, financial condition and results of operations.

We rely heavily on technology, particularly the internet, to provide high-quality online services. However, our technology operations are vulnerable to disruptions arising from human error, natural disasters, power failure, computer viruses, spam attacks, unauthorized access and other similar events. Disruptions to, or instability of, our technology or external technology that allows our pharmacy customers and consumers to use our online services and products could materially harm our business and reputation.

Although we have employed significant resources to develop security measures against breaches, our cybersecurity measures may not detect or prevent all attempts to compromise our systems, including distributed denial-of-service attacks, viruses, malicious software, break-ins, phishing attacks, social engineering, misconduct or sabotage by our employees, security breaches or other attacks and similar disruptions that may jeopardize the security of information stored in and transmitted by our systems or that we otherwise maintain. Breaches of our cybersecurity measures could result in unauthorized access to our systems, misappropriation of information or data, deletion or modification of user information, or a denial-of-service or other interruption to our business operations. As techniques used to obtain unauthorized access to or sabotage systems change frequently and may not be known until launched against us, we may be unable to anticipate, or implement adequate measures to protect against, these attacks. There can be no assurance that we would not in the future be subject to such attacks that may result in material damages or remediation costs. If we are unable to avert these attacks and security breaches, we could be subject to significant legal and financial liability, our reputation would be harmed and we could sustain substantial revenue loss from lost sales and customer dissatisfaction.

In addition, we may not have the resources or technical sophistication to anticipate or prevent rapidly evolving types of cyber-attacks. Cyber-attacks may target us, our users or other participants of our ecosystem, or the information infrastructure on which we depend. Actual or anticipated attacks and risks may cause us to incur significantly higher costs, including costs to deploy additional personnel and network protection technologies, train employees, and engage third-party experts and consultants. Cybersecurity breaches may harm our reputation and business, and materially and adversely affect our financial condition and results of operations.

Our failure to comply with anti-corruption laws and regulations, or effectively manage our employees, marketplace sellers and affiliates, could severely damage our reputation, and materially and adversely affect our business, financial condition, results of operations and prospects.

We are subject to risks in relation to actions taken by us, our employees, marketplace sellers or affiliates that constitute violations of the anti-corruption laws and regulations. There have been several instances of corrupt practices in the pharmaceutical industry, including, among other things, receipt of kickbacks, bribes or other illegal gains or benefits by pharmacies, hospitals and medical practitioners from manufacturers, distributors and retail pharmacies in connection with the prescription of pharmaceutical products. While we adopt strict internal procedures and work closely with relevant government agencies to ensure compliance of our business operations with relevant laws and regulations, our efforts may not be sufficient to ensure that we comply with relevant laws and regulations at all times. If we, our employees, marketplace sellers or affiliates violate these laws, rules or regulations, we could be subject to fines and/or other penalties. In the case of our retail and wholesale businesses, the products involved may be seized and our operations may be suspended. Actions by PRC regulatory authorities or the courts to provide an interpretation of PRC laws and regulations that differs from our interpretation or to adopt additional anti-bribery or anti-corruption related regulations could also require us to make changes to our operations. Our reputation, corporate image, and business operations may be materially and adversely affected if we fail to comply with these measures or become the target of any negative publicity as a result of actions taken by us, our employees, marketplace sellers or affiliates, which may in turn have a material adverse effect on our business, financial condition, results of operations and prospects.

Our delivery, return and exchange policies may materially and adversely affect our results of operations.

We have adopted shipping policies that do not necessarily pass the full cost of shipping on to our pharmacy customers and consumers. We have also adopted policies that permit the return and exchange of our products within thirty days in certain circumstances for specified reasons. We may also be required by law to adopt new or amend existing return and exchange policies from time to time. For example, pursuant to the Consumer Protection Law and relevant regulations and rules, consumers are generally entitled to return products purchased within seven days upon receipt without reason when they purchase the products from business operators on the internet with certain exception, such as pharmaceutical products. These policies subject us to additional costs and expenses which we may not recoup through increased revenue. Our ability to handle a large volume of returns is unproven. If we revise these policies to reduce our costs and expenses, our pharmacy customers and consumers may be dissatisfied, which may result in loss of existing consumers and pharmacy customers or failure to acquire new consumers and pharmacy customers at a desirable pace, which may materially and adversely affect our results of operations.

If we are subject to higher product return rates, our business, financial condition and results of operations may be materially and adversely affected.

We have established a thirty-day product return policy in certain circumstances for specified reasons. In addition, pursuant to the Consumer Protection Law, consumers are generally entitled to return purchased products within seven days upon receipt without giving any reasons when they purchase the products from business operators on the internet. Although a majority of our products may not be returned or exchanged under the Administrative Standard of Pharmaceutical Operating Quality, prohibiting returns and exchanges of pharmaceutical products except for quality reasons, if our product return rates increase or are higher than expected, our revenues and costs can be negatively impacted. Furthermore, as we cannot return some products to our suppliers pursuant to our contracts with them or if return rates for such products increase significantly, we may experience an increase in our inventory balance, inventory impairment and fulfillment cost, which may materially and adversely affect our working capital. As a result, our business, financial condition and results of operations may be materially and adversely affected.

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We may not be able to conduct our marketing activities effectively, properly, or at reasonable costs, and we are subject to limitations in promoting our services and products, which will have an impact on our business operations.

We invest significant resources in a variety of different marketing and brand promotion efforts designed to enhance our brand recognition and increase sales of our services and products. However, our brand promotion and marketing activities may not be well received and may not result in the levels of sales that we anticipate. Meanwhile, marketing approaches and tools in the PRC internet healthcare market are continually evolving, which may further require us to enhance our marketing approaches and experiment with new marketing methods to keep pace with industry developments and customer preferences. Failure to refine our existing marketing approaches or to introduce new marketing approaches in a cost-effective manner could reduce our market share and materially and adversely affect our financial condition, results of operations and profitability. In addition, we are subject to certain limitations in promoting services and products. Our in-house medical team and external doctors and other relevant parties in the provision of our medical and wellness services have to comply with rules and regulations that restrict the promotion or dissemination of information about the professional healthcare services and practice provided by licensed doctors, and the publication or marketing efforts for the predominant purpose of promoting the products or services of doctors to consumers or potential consumers. Such restrictions may affect our ability to further enhance our brand recognition or secure new business opportunities in the future.

Under PRC laws and regulations, all advertisements published online containing drug names, applicable symptoms treated by such drugs (major functions) or other drug-related content, and advertisements published online containing medical device names and the applicable scope, performance, structure and composition, function and other contents relevant to medical device are subject to examination by relevant government authorities. We are prohibited from publishing advertisements of prescription drugs on our website and must ensure that any advertisement of medical treatment, drugs or medical devices does not include any assertion or guarantee as to the function and safety or any statement of curative rate and effectiveness of such medical treatment, drugs or medical devices. Any violation of advertisement-related laws and regulations may subject us to fine, or even suspension of our business or revocation of our business license. See “Item 4. Information on the Company—B. Business Overview—Regulations—Regulations Relating to Online Advertising.” Although we have implemented internal procedures to examine the content of advertisements displayed on our website, we cannot assure you that all such content meets the requirements under PRC advertising-related laws and regulations at all times. In the past, we have been required to pay penalties for advertisements displayed on our website due to non-compliance with advertising laws.

There can be no assurance that our existing practices of monitoring our information dissemination process and publication would continue to be effective and would comply fully with laws and regulations. Should there be any change in the relevant rules and regulations, or change of interpretation thereof, we, our in-house medical team, external doctors and other relevant third parties may be regarded as breaching the relevant rules and regulations and may be subject to regulatory penalties or disciplinary actions, which may materially and adversely affect our business and reputation.

We may not be able to detect or prevent fraud or other misconduct committed by our employees or third parties.

Fraud or other misconduct by our employees, such as unauthorized business transactions, bribery and breach of our internal policies and procedures, unauthorized access to or leakage of the data of our consumers and pharmacy customers, or by third parties, such as breach of law, may be difficult to detect or prevent. It could subject us to financial loss and sanctions imposed by governmental authorities while seriously damaging our reputation. This may also impair our ability to effectively attract prospective users, develop customer loyalty, obtain financing on favorable terms and conduct other business activities.

In particular, we may face risks with respect to fictitious or other fraudulent activities. There can be no assurance that the measures we have implemented to detect and reduce the occurrence of fraudulent activities would be effective in combating fraudulent transactions or improving overall satisfaction among our consumers and pharmacy customers, pharmaceutical companies and marketplace sellers. Our marketplace sellers may also engage in fictitious or “phantom” transactions with themselves or collaborators in order to artificially inflate their ratings, reputation and search results rankings. This activity may harm other third parties by enabling the perpetrating marketplace seller to be favored over legitimate ones, may harm consumers by deceiving them into believing that a marketplace seller is more reliable or trusted than that marketplace seller actually is, and result in inflated GMV from our online marketplace.

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Our risk management systems, information technology systems and internal control procedures are designed to monitor our operations and overall compliance. However, we may be unable to identify non-compliance or suspicious transactions promptly, or at all. Furthermore, it is not always possible to detect and prevent fraud or other misconduct committed by our employees, ecosystem participants or other third parties, and the precautions we take to prevent and detect such activities may not be effective. Therefore, we are subject to the risk that fraud or other misconduct may have previously occurred but was undetected, or may occur in the future. This may materially and adversely affect our business, financial condition and results of operations.

Our business operations and financial performance have been adversely affected by the COVID-19 outbreak, may in the future continue to be affected by the COVID-19 outbreak and recurrence, and may be affected by other natural disasters, epidemics and other unforeseeable catastrophes.

Since the end of December 2019, the outbreak of COVID-19 has materially and adversely affected the global economy. The COVID-19 pandemic caused disruptions to our business operations and those of our customers, suppliers, and logistics providers, to varying degrees. For example, the COVID-19 had caused companies in China, including us and certain of our customers and suppliers, to implement temporary adjustment of work schedules and travel plans or to require employees to work from home and collaborate remotely, resulting in compromised efficiency and productivity. While the pandemic has come under control in the PRC since the second quarter of 2020, there was a significant rise in COVID-19 cases, including the COVID-19 Delta and Omicron variant cases, in various cities in China in early 2022. The local governments of the affected cities have reinstated certain COVID-related measures, including travel restrictions and stay-at-home orders. Our results of operations may be adversely affected by COVID-19 if more cities and regions implement similar anti-COVID measures and the pandemic continues to affect the Chinese economy in general. The extent to which COVID-19 impacts our financial position, results of operations and cash flows in future periods will depend on the future developments of the pandemic, including any potential future variants of the virus, the effectiveness of the mass vaccination programs, the development in medical treatment and other actions taken to contain its spread, which are highly uncertain and unpredictable. If there is not a material recovery in the COVID-19 situation, or the situation further deteriorates in China, our business, results of operations and financial condition could be materially and adversely affected.

We may need additional capital but may not be able to obtain it on favorable terms or at all.

We may require additional cash resources due to operating losses or future growth and development of our business, including any investments or acquisitions we may decide to pursue. If our cash resources are insufficient to satisfy our cash requirements, we may seek to issue additional equity or debt securities or obtain new or expanded credit facilities. Our ability to obtain external financing in the future is subject to a variety of uncertainties, including our future financial condition, results of operations, cash flows, share price performance, liquidity of international capital and lending markets and the PRC governmental regulations over foreign investment and the PRC healthcare industry. In addition, incurring indebtedness would subject us to increased debt service obligations and could result in operating and financing covenants that would restrict our operations. There can be no assurance that financing would be available in a timely manner or in amounts or on terms favorable to us, or at all. Any failure to raise needed funds on terms favorable to us, or at all, could severely restrict our liquidity as well as have a material adverse effect on our business, financial condition and results of operations. Moreover, any issuance of equity or equity-linked securities could result in significant dilution to our existing shareholders. See "Item 5. Operating and Financial Review and Prospects—B. Liquidity and Capital Resources."

Our business could be disrupted by network interruptions.

Our business depends on the efficient and uninterrupted operation of our computer and communications systems and our entire information infrastructure is located in China. Our information infrastructure contains substantial quantities of data relating to our supply chain information, competitive pricing data and customer base, such as customer behavior, consultation records and transaction data, among other things, which enable our users to access the full range of our services and other ecosystem participants to conduct their operations efficiently and effectively over our platforms. Although we have certain precautions to address potential interruptions, such preparation may not be sufficient and we do not carry business interruption insurance. Furthermore, despite any precautions we may take, the occurrence of a natural disaster, such as an earthquake, flood or fire, or other unanticipated incidents at our information infrastructure facilities in China, including power outages, telecommunications delays or failures, break-ins to our systems or computer viruses, could result in delays or interruptions to our platform and operations as well as loss of our consumers' and other participants' data. Any of these events could damage our reputation, materially disrupt our ecosystem and subject us to liability and claims, which may materially and adversely affect our business, financial condition and results of operations.

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An occurrence of a natural disaster, widespread health epidemic or other outbreaks could have a material adverse effect on our business, financial condition and results of operations.

Our business could be materially and adversely affected by natural disasters, such as snowstorms, earthquakes, fires or floods, the outbreak of a widespread health epidemic or other events, such as wars, acts of terrorism, environmental accidents, power shortage, labor unrest or communication interruptions. The occurrence of such a disaster or prolonged outbreak of an epidemic illness or other adverse public health developments in the PRC or elsewhere could materially disrupt our business and operations. Such events could also significantly affect our industry and cause a temporary closure of the facilities we use for our operations, which would severely disrupt our operations and have a material adverse effect on our business, financial condition and results of operations. Our operations could be disrupted if any of our employees were suspected of having any of the epidemic illnesses, since this could require us to quarantine some or all of such employees or disinfect the facilities used for our operations. In addition, our revenue and profitability could be materially reduced to the extent that a natural disaster, health epidemic or other outbreak harms the global or PRC economy in general. Our operations could also be severely disrupted if our users or other participants were affected by such natural disasters, health epidemics or other outbreaks. See also “ - Our business operations and financial performance have been adversely affected by the COVID-19 outbreak, may in the future continue to be affected by the COVID-19 outbreak, and may be affected by other natural disasters, epidemics and other unforeseeable catastrophes.”

Risks Related to Doing Business in China

Changes in China's economic, political or social conditions or government policies could have a material adverse effect on our business and results of operations.

Substantially all of our operations are located in China. Accordingly, our business, prospects, financial condition and results of operations may be influenced to a significant degree by political, economic and social conditions in China generally and by continued economic growth in China as a whole.

The Chinese economy differs from the economies of most developed countries in many respects, including the amount of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. Although the Chinese government has implemented measures emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets and the establishment of improved corporate governance in business enterprises, a substantial portion of productive assets in China are still owned by the government. In addition, the Chinese government continues to play a significant role in regulating industry development by imposing industrial policies. The Chinese government also exercises significant control over China's economic growth through allocating resources, controlling payment of foreign currency-denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies.

While the Chinese economy has experienced significant growth over the past decades, growth has been uneven, both geographically and among various sectors of the economy. The Chinese government has implemented various measures to encourage economic growth and guide the allocation of resources. Some of these measures may benefit the overall Chinese economy, but may have a negative effect on us. For example, our financial condition and results of operations may be adversely affected by government control over capital investments or changes in tax regulations. In addition, in the past the Chinese government has implemented certain measures, including interest rate increases, to control the pace of economic growth. These measures may cause decreased economic activity in China, and since 2012, the Chinese economy has slowed down. Any prolonged slowdown in the Chinese economy may reduce the demand for our products and services and materially and adversely affect our business and results of operations.

Uncertainties in the interpretation and enforcement of PRC laws and regulations and sudden or unexpected changes in policies, laws and regulations in China could limit the legal protections available to us.

The PRC legal system is based on written statutes and prior court decisions have limited value as precedents. Since these laws and regulations are relatively new and the PRC legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform and enforcement of these laws, regulations and rules involves uncertainties.

The PRC government has significant oversight and discretion over the conduct of our business and may intervene with or influence our operations as it deems appropriate to further regulatory, political and societal goals. The PRC government has recently published new policies that affected our industry, and we cannot rule out the possibility that it will in the future further release regulations or policies regarding our industry that could further adversely affect our business, financial condition and results of operations. Furthermore, the PRC government has also recently published new regulations and guidance to exert more oversight and control over securities offerings and other capital markets activities that are conducted overseas and foreign investment in China-based companies like us. Any such action, once taken by the PRC government, could significantly limit or completely hinder our ability to offer or continue to offer securities to investors and cause the value of such securities to significantly decline or in extreme cases, become worthless. We cannot assure you that we will be able to comply with these new laws and regulations in all respects, and we may be ordered to rectify, suspend or terminate any actions or services that are deemed illegal by the regulatory authorities and become subject to material penalties, which may materially harm our business, financial condition, results of operations and prospects.

From time to time, we may have to resort to administrative and court proceedings to enforce our legal rights. However, since PRC administrative and court authorities have significant discretion in interpreting and implementing statutory and contractual terms, it may be more difficult to evaluate the outcome of administrative and court proceedings and the level of legal protection we enjoy than in more developed legal systems. Furthermore, the PRC legal system is based in part on government policies and internal rules (some of which are not published in a timely manner or at all) that may have retroactive effect. As a result, we may not be aware of our violation of these policies and rules until sometime after the violation. Such uncertainties, including uncertainty over the scope and effect of our contractual, property (including intellectual property) and procedural rights, could materially and adversely affect our business and impede our ability to continue our operations.

The approval, filing or other requirements of the China Securities Regulatory Commission or other PRC government authorities may be required under PRC law in connection with our issuance of securities overseas.

The Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, or the M&A Rules, purport to require offshore special purpose vehicles that are controlled by PRC companies or individuals and that have been formed for the purpose of seeking a public listing on an overseas stock exchange through acquisitions of PRC domestic companies or assets to obtain CSRC approval prior to publicly listing their securities on an overseas stock exchange. The interpretation and application of the regulations remain unclear. If CSRC approval under the M&A Rules is required, it is uncertain whether it would be possible for us to obtain the approval, and any failure to obtain or delay in obtaining CSRC approval for our future issuance of securities overseas would subject us to sanctions imposed by the CSRC and other PRC regulatory agencies.

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Furthermore, the recently issued Opinions on Strictly Cracking Down on Illegal Securities Activities emphasized the need to strengthen the administration over “illegal securities activities” and the supervision on overseas listings by China-based companies, and proposed to take effective measures, such as promoting the construction of relevant regulatory systems to deal with the risks and incidents faced by China-based overseas-listed companies, although such opinions did not specify the definition of “illegal securities activities.” On December 24, 2021, the CSRC published the draft Administrative Provisions of the State Council on the Overseas Issuance and Listing of Securities by Domestic Companies (Draft for Comments), or the Draft Overseas Listing Regulations, and the draft Measures for the Overseas Issuance and Listing of Securities Record-filings by Domestic Companies (Draft for Comments), the Draft Overseas Listing Measures, for public comments. These draft regulations stipulate that PRC domestic companies that seek to offer and list securities in overseas markets directly or indirectly shall complete the filing procedures with and report relevant information to the CSRC. Pursuant to these draft rules, if the issuer meets the following conditions, its securities offerings and listing will be deemed as an “indirect overseas offering and listing by a PRC domestic company” and is therefore subject to the filing requirement: (i) the revenues, profits, total assets or net assets of the Chinese operating entities in the most recent financial year accounts for more than 50% of the corresponding data in the issuer’s audited consolidated financial statements for the same period; (ii) the majority of senior management in charge of business operation are Chinese citizens or have domicile in PRC, and its principal place of business is located in PRC or main business activities are conducted in PRC. In addition, these draft rules prescribe that the domestic enterprises submit filing documents to CSRC within three business days after the submission of the application for overseas initial public offering, and after completing the filing procedures for an overseas initial public offering and listing, for the purposes of implementing and strengthening the CSRC’s supervision, the issuer will need to comply with continuous filing and reporting requirements after such offering and listing, among others, including the following: (i) reporting material events which arose prior to such offering and listing, (ii) filing for follow-on offerings after the initial offering and listing, (iii) filing for transactions in which the issuer issues securities to acquire assets, and (iv) reporting material events after the initial offering and listing. However, the Draft Overseas Listing Regulations and the Draft Overseas Listing Measures were released for public comment only, there remains substantial uncertainty, including but not limited to its final content, adoption timeline, effective date or relevant implementation rules. As of the date of this annual report, we cannot predict the impact of these regulations on maintain the listing status of our ADSs and/or other securities, or any of our future offerings of securities overseas in a foreign country.

In addition, in December 2021, the CAC and several other regulatory authorities in China jointly promulgated the Cybersecurity Review Measures, which came into effect in February 2022. Pursuant to the Cybersecurity Review Measures, (i) if the relevant activity affects or may affect national security, a CIIO that purchases network products and services, or an internet platform operator that conducts data process activities, shall be subject to the cybersecurity review, (ii) an application for cybersecurity review shall be made by an issuer who is an internet platform operator holding personal information of more than one million users before such issuer applies to list its securities on a foreign stock exchange, and (iii) relevant governmental authorities in the PRC may initiate cybersecurity review if they determine an operator’s network products or services or data processing activities affect or may affect national security. As the Cybersecurity Review Measures was newly issued, there remain uncertainties as to how it would be interpreted and enforced, and to what extent it may affect us.

If the CSRC or other relevant PRC regulatory agencies subsequently determine that prior approval is required for any of our future offerings of securities overseas or to maintain the listing status of our ADSs, we cannot guarantee that we will be able to obtain such approval in a timely manner, or at all. The CSRC or other PRC regulatory agencies also may take actions requiring us, or making it advisable for us, not to proceed with such offering or maintain the listing status of our ADSs. If we proceed with any of such offering or maintain the listing status of our ADSs without obtaining these regulatory agencies’ approval to the extent it is required, or if we are unable to comply with any new approval requirements which might be adopted for offerings that we have completed prior to the publication of the above- referenced opinions, we may face regulatory actions or other sanctions from these regulatory agencies.

These regulatory agencies may impose fines and penalties on our operations in China, limit our ability to pay dividends outside of China, limit our operating privileges in China, delay or restrict the repatriation of the proceeds from offering of securities overseas into China or take other actions that could have a material adverse effect on our business, financial condition, results of operations and prospects, as well as the trading price of the ADSs.

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Furthermore, if there are any other approvals, filings and/or other administration procedures to be obtained from or completed with the CSRC or other PRC regulatory agencies as required by any new laws and regulations for any of our future proposed offering of securities overseas or the listing of the ADSs, we cannot assure you that we can obtain the required approval or complete the required filings or other regulatory procedures in a timely manner, or at all. Any failure to obtain the relevant approvals or complete the filings and other relevant regulatory procedures may subject us to regulatory actions or other sanctions from the CSRC or other PRC regulatory agencies, which may have a material adverse effect on our business, financial condition or results of operations.

We may be adversely affected by the complexity, uncertainties and changes in PRC regulation of pharmaceutical and healthcare industry and internet-related businesses, and any lack of requisite approvals, licenses or permits applicable to our business may have a material adverse effect on our business and results of operations.

Our business is subject to governmental supervision and regulation by the relevant PRC governmental authorities, including but not limited to the MOFCOM, the MIIT, the National Medical Products Administration, or the NMPA, the NHC and the SAMR and their counterparts. Together, these government authorities promulgate and enforce regulations that cover many aspects of the operation of pharmaceutical operation, medical and healthcare services and internet-related business, including foreign ownership of, and the licensing and permit requirements pertaining to, companies in such business. The laws and regulations related to medical and healthcare services and internet-related business are evolving rapidly, and their interpretation and enforcement involve significant uncertainties. As a result, in certain circumstances it may be difficult to determine what actions or omissions may be deemed to be in violation of applicable laws and regulations. Under PRC laws, an entity must obtain the pharmaceutical operation license from the NMPA or its counterpart for conducting pharmaceutical wholesale and retail business, the value-added telecommunication service operating licenses from the MIIT or its counterpart for either online information services or third-party e-commerce platform, and a medical institution shall obtain a practicing license of medical institutions from the NHC for provision of medical diagnosis and treatment services. We have made great efforts to obtain all applicable licenses and permits necessary to our main business. However, the interpretation and application of existing PRC laws, regulations and policies and possible new laws, regulations or policies relating to the pharmaceutical operation, medical and healthcare services and internet-related business have created substantial uncertainties regarding the legality of existing and future foreign investments in, and the businesses and activities of, pharmaceutical operation, medical and healthcare services and internet-related business industry in China, including our business, we cannot assure you that we have obtained all the permits or licenses required for conducting our business or will be able to maintain our existing licenses or obtain new ones. If the PRC government considers that we were operating without the proper approvals, licenses or permits or promulgates new laws and regulations that require additional approvals or licenses or imposes additional restrictions on the operation of any part of our business, it has the power, among other things, to levy fines, confiscate our income, revoke our business licenses, and require us to discontinue our relevant business or impose restrictions on the affected portion of our business. Any of these actions by the PRC government may have a material adverse effect on our business and results of operations.

We rely on dividends and other distributions on equity paid by our PRC subsidiaries to fund any cash and financing requirements we may have, and any limitation on the ability of our PRC subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our business.

We are a holding company, and we rely on dividends and other distributions on equity paid by our PRC subsidiaries for our cash and financing requirements, including the funds necessary to pay dividends and other cash distributions to our shareholders and service any debt we may incur. If our PRC subsidiaries incur debt on their own behalf in the future, the instruments governing the debt may restrict their ability to pay dividends or make other distributions to us, which may restrict our ability to satisfy our liquidity requirements.

Under PRC laws and regulations, our PRC subsidiaries may pay dividends only out of their accumulated after-tax profits as determined in accordance with PRC accounting standards and regulations. In addition, Chinese entities are required to set aside at least 10% of their accumulated after-tax profits each year, if any, to fund certain statutory reserve funds, until the aggregate amount of such funds reaches 50% of their registered capital. These reserve funds are not distributable as cash dividends.

At the end of 2016, the People's Bank of China, or PBOC, and the State Administration of Foreign Exchange, or SAFE, implemented a series of capital control measures, including stricter vetting procedures for China-based companies to remit foreign currency for overseas acquisitions, dividend payments and shareholder loan repayments. For instance, the PBOC issued the Circular on Further Clarification of Relevant Matters Relating to Offshore Renminbi Loans Provided by Domestic Enterprises, in November 2016, which provides that offshore Renminbi loans provided by a domestic enterprise to offshore enterprises that are its affiliates in equity shall not exceed a certain amount that is equal to the most recent audited owner's equity multiplied by a ratio determined by the PBOC, and may constrain our PRC subsidiaries' ability to provide offshore loans to us. The PRC government may continue to strengthen its capital controls and our PRC subsidiaries' dividends and other distributions or payment may be subjected to tighter scrutiny in the future. Any limitation on the ability of our PRC subsidiaries to pay dividends or make other distributions or make payments to us could materially and adversely limit our ability to grow, make investments or acquisitions that could be beneficial to our business, pay dividends, or otherwise fund and conduct our business. See also “—If we are classified as a PRC resident enterprise for PRC income tax purposes, such classification could result in unfavorable tax consequences to us and our non-PRC shareholders or ADS holders.”

PRC regulation of loans to and direct investment in PRC entities by offshore holding companies and governmental control of currency conversion may delay or prevent us from using the proceeds of our initial public offering to make loans to or make additional capital contributions to our PRC subsidiaries, which could materially and adversely affect our liquidity and our ability to fund and expand our business.

We are an offshore holding company conducting our operations in China through our PRC subsidiaries. We may make loans to our PRC subsidiaries subject to the approval from governmental authorities and limitation of amount, or we may make additional capital contributions to our foreign invested subsidiaries in China.

Any funds we transfer to our PRC subsidiaries, either as a shareholder loan or as an increase in registered capital, are subject to filing or registration with the relevant governmental authorities in China. According to the relevant PRC regulations on foreign-invested enterprises in China, capital contributions to our PRC subsidiaries are subject to the requirement of making necessary filings and registration with other governmental authorities in China. In addition, (a) any foreign loan procured by our PRC subsidiaries is required to be registered with SAFE, or its local branches, and (b) each of our PRC subsidiaries may not procure loans which exceed the statutory limit. We may not complete such recording or registrations on a timely basis, if at all, with respect to future capital contributions or foreign loans by us to our PRC subsidiaries. If we fail to complete such recording or registration, our ability to use the proceeds of our initial public offering and to capitalize our PRC operations may be negatively affected, which could adversely affect our liquidity and our ability to fund and expand our business.

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In 2008, SAFE promulgated the Notice of the General Affairs Department of the State Administration of Foreign Exchange on the Relevant Operating Issues concerning the Improvement of the Administration of Payment and Settlement of Foreign Currency Capital of Foreign-invested Enterprises, or Circular 142, which used to regulate the conversion by foreign-invested enterprises of foreign currency into Renminbi by restricting the usage of converted Renminbi. In March 2015, SAFE promulgated the Notice of the State Administration of Foreign Exchange on Reforming the Administrative Approach Regarding the Settlement of the Foreign Exchange Capitals of Foreign-invested Enterprises, or Circular 19. Circular 19 took effect as of June 1, 2015 and superseded Circular 142 on the same date. Circular 19 launched a nationwide reform of the administration of the settlement of the foreign exchange capitals of foreign-invested enterprises and allows foreign-invested enterprises to settle their foreign exchange capital at their discretion, but continues to prohibit foreign-invested enterprises from using the Renminbi fund converted from their foreign exchange capitals for expenditures beyond their business scopes. In June 2016, SAFE promulgated the Notice of the State Administration of Foreign Exchange on Reforming and Standardizing the Administrative Provisions on Capital Account Foreign Exchange Settlement, or Circular 16. Circular 16 continues to prohibit foreign-invested enterprises from, among other things, using the Renminbi fund converted from its foreign exchange capitals for expenditure beyond its business scope, investment and financing (except for guarantee products issued by a bank or otherwise permitted by laws), providing loans to non-affiliated enterprises or constructing or purchasing real estate not for self-use (except for real estate enterprise). Pursuant to the Notice of the State Administration of Foreign Exchange on Further Promoting Cross-border Trade and Investment Facilitation, or Circular 28, promulgated on October 23, 2019, non-investment foreign invested enterprises are allowed to invest their capital in domestic equity in accordance with laws and regulations on the condition that such investment is not in violation of the Special Administrative Measures for Admission of Foreign Investment (Negative List) in force and the domestic projects to be invested shall be authentic and legal. According to the Circular on Optimizing the Administration of Foreign Exchange to Support the Development of Foreign-related Business, or SAFE Circular 8, issued by the SAFE on April 10, 2020, eligible enterprises are allowed to make domestic payments using the income under their capital accounts generated from their capital, foreign debt and overseas listing, without providing materials evidencing the authenticity in advance, provided that the capital usage is authentic and compliant with the current capital account income usage management regulations. The concerned bank is required to conduct spot checks in accordance with the relevant requirements. However, as these circulars are relatively new, there are still uncertainties regarding its interpretation, implementation and enforcement. All of these factors may significantly limit our ability to transfer to and use in China the net proceeds from our initial public offering, which may adversely affect our business, financial condition and results of operations.

Fluctuations in exchange rates could have a material adverse effect on our results of operations and the price of the ADSs.

The value of the Renminbi against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in political and economic conditions in China and by China's foreign exchange policies. In July 2005, the PRC government changed its decade-old policy of pegging the value of the Renminbi to the U.S. dollar, and the Renminbi appreciated more than 20% against the U.S. dollar over the following three years. Between July 2008 and June 2010, this appreciation halted and the exchange rate between the Renminbi and the U.S. dollar remained within a narrow band. Since June 2010, Renminbi has fluctuated against the U.S. dollar, at certain times significantly and unpredictably. With the development of the foreign exchange market progressing towards interest rate liberalization and Renminbi internationalization and economic uncertainties in both China and the rest of the world, the PRC government may in the future announce further changes to the exchange rate system and we cannot assure you that the Renminbi will not appreciate or depreciate significantly in value against the U.S. dollar in the future. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between the Renminbi and the U.S. dollar in the future.

All of our revenue and substantially all of our costs are denominated in Renminbi and our reporting currency is Renminbi. Significant revaluation of the Renminbi may have a material and adverse effect on your investment. For example, to the extent that we need to convert U.S. dollars we received from our initial public offering into Renminbi for our operations, appreciation of the Renminbi against the U.S. dollar would reduce the Renminbi amount we would receive from the conversion. Conversely, if we decide to convert our Renminbi into U.S. dollars for the purpose of making payments for dividends on our ordinary shares or ADSs or for other business purposes, appreciation of the U.S. dollar against the Renminbi would reduce the U.S. dollar amount available to us.

Very limited hedging options are available in China to reduce our exposure to exchange rate fluctuations. To date, we have not entered into any hedging transactions in an effort to reduce our exposure to foreign currency exchange risk. While we may decide to enter into hedging transactions in the future, the availability and effectiveness of these hedges may be limited and we may not be able to hedge our exposure adequately or at all. In addition, our currency exchange losses may be magnified by PRC exchange control regulations that restrict our ability to convert Renminbi into foreign currency.

Governmental control of currency conversion may limit our ability to utilize our operating revenue effectively and affect the value of your investment.

The PRC government imposes controls on the convertibility of the Renminbi into foreign currencies and, in certain cases, the remittance of currency out of China. We receive substantially all of our operating revenue in Renminbi. Under our current corporate structure, our company in the Cayman Islands relies on dividend payments from our PRC subsidiaries to fund any cash and financing requirements we may have.

Under existing PRC foreign exchange regulations, payments of current account items, such as profit distributions and trade and service-related foreign exchange transactions, can be made in foreign currencies without prior approval from SAFE by complying with certain procedural requirements. Therefore, our PRC subsidiary, 1 Pharmacy Technology, is able to pay dividends in foreign currencies to us without prior approval from SAFE, subject to the certain procedures under PRC foreign exchange regulation. But approval from or registration with appropriate government authorities is required where Renminbi is to be converted into foreign currency and remitted out of China to pay capital expenses under capital account items such as overseas investment and the repayment of loans denominated in foreign currencies.

In light of the substantial capital outflows of China in 2016 due to the weakening of Renminbi, the PRC government has imposed more restrictive foreign exchange policies and stepped up scrutiny of major outbound capital movement. More restrictions and substantial vetting processes have been put in place by SAFE to regulate cross-border transactions falling under the capital account. The PRC government may at its discretion further restrict access to foreign currencies in the future for current account transactions. If the foreign exchange control system prevents us from obtaining sufficient foreign currencies to satisfy our foreign currency demands, we may not be able to pay dividends in foreign currencies to our shareholders, including holders of our ADSs.

Failure to make adequate contributions to various employee benefit plans and withhold individual income tax on employees' salaries as required by PRC regulations may subject us to penalties.

Companies operating in China are required to participate in various government-mandated employee benefit contribution plans, including certain social insurance, housing funds and other welfare-oriented payment obligations, and contribute to the plans in amounts equal to certain percentages of salaries, including bonuses and allowances, of our employees up to a maximum amount specified by the local government from time to time at locations where we operate our businesses. The requirement of employee benefit contribution plans has not been implemented consistently by the local governments in China given the different levels of economic development in different locations. Companies operating in China are also required to withhold individual income tax on employees' salaries based on the actual salary of each employee upon payment. We may be subject to late fees and fines in relation to the underpaid employee benefits and under-withheld individual income tax, our financial condition and results of operations may be adversely affected.

The M&A Rules and certain other PRC regulations establish complex procedures for some acquisitions of Chinese companies by foreign investors, which could make it more difficult for us to pursue growth through acquisitions in China.

The Regulations on Mergers and Acquisitions of Domestic Companies by Foreign Investors, or the M&A Rules, adopted by six PRC regulatory agencies in 2006 and amended in 2009, and some other regulations and rules concerning mergers and acquisitions, established additional procedures and requirements that could make merger and acquisition activities by foreign investors more time-consuming and complex, including requirements in some instances that the MOFCOM be notified in advance of any change-of-control transaction in which a foreign investor takes control of a PRC domestic enterprise. Moreover, the Anti-Monopoly Law of the People's Republic of China requires that the MOFCOM shall be notified in advance of any concentration of undertaking if certain thresholds are triggered. On February 7, 2021, the SAMR further issued the Anti-Monopoly Guidelines for the Internet Platform Economy Sector that aims at specifying some of the circumstances under which an activity of internet platforms may be identified as monopolistic act as well as setting out merger controlling filing procedures involving variable interest entities.

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In addition, a regulation related to security review on mergers and acquisitions of domestic enterprise by foreign investors issued by the MOFCOM that became effective in September 2011 specifies that mergers and acquisitions by foreign investors that raise “national defense and security” concerns and mergers and acquisitions through which foreign investors may acquire de facto control over domestic enterprises that raise “national security” concerns are subject to strict review by the MOFCOM, and the rules prohibit any activities attempting to bypass a security review, including by structuring the transaction through a proxy or contractual control arrangement. In December 2020, the NDRC and the MOFCOM further promulgated the Foreign Investment Security Review Measures, which took effect on January 18, 2021. These measures require direct or indirect investment by foreign investors of PRC companies engaged in military-related or certain other industries be subject to security review before consummation of any such investment. “Certain other industries” refer to, among others, important transportation services, important culture products and services, important information technology and internet products and services, and important finance services that are crucial to national security. In the future, we may grow our business by acquiring complementary businesses. Complying with the requirements of the above-mentioned regulations and other relevant rules to complete such transactions could be time-consuming, and any required approval processes, including obtaining approval from the MOFCOM or its local counterparts may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business or maintain our market share.

PRC regulations relating to offshore investment activities by PRC residents may limit our PRC subsidiaries’ ability to increase their registered capital or distribute profits to us or otherwise expose us or our PRC resident beneficial owners to liability and penalties under PRC law.

In October 2005, SAFE issued a circular on relevant issues relating to foreign exchange administration in fund financing and roundtrip investment by domestic residents via offshore special purpose vehicles, or Circular 75, requiring PRC residents, including individual and entities, to register with the relevant local branch of SAFE before establishing or controlling any company outside of China, referred to as an offshore special purpose company, for the purpose of raising funds from overseas to acquire or exchange assets of, or acquiring equity interest in, PRC companies held by such PRC residents.

In July 2014, the SAFE issued a circular on foreign exchange administration involved in overseas investment, financing and roundtrip investment conducted by PRC residents via offshore special purpose vehicles, or Circular 37, which replaced Circular 75 and further requires PRC residents or entities to register with SAFE or its local branch in connection with their establishment or control of an offshore entity established for the purpose of overseas investment or financing by either onshore or offshore assets or equity legally held by such PRC residents. In February 2015, SAFE released the Notice of the State Administration of Foreign Exchange on Further Simplifying and Improving the Policies of Foreign Exchange Administration Applicable to Direct Investment, or Circular 13, which further clarified that offshore individuals who have foreign identification and use their offshore assets or equity to make contributions into an offshore special vehicle are not subject to the registration under Circular 37.

If our shareholders who are PRC residents or entities do not complete their registration as required, our PRC subsidiary, 1 Pharmacy Technology, may be prohibited from distributing their profits and proceeds from any reduction in capital, share transfer or liquidation to us, and we may be restricted in our ability to contribute additional capital to our PRC subsidiaries. Moreover, failure to comply with the SAFE registration described above could result in liability under PRC laws for evasion of applicable foreign exchange restrictions.

Since Dr. Gang Yu and Mr. Junling Liu are non-PRC citizens with foreign identification who establish and make contributions to our Cayman Islands holding company by their offshore assets, they are not subject to the foreign exchange registrations for their offshore investment, financing and roundtrip investment in accordance with Circular 75 then in effect and Circular 37.

However, we may not be informed of the identities of all PRC residents holding direct or indirect interest in our company, nor can we compel our beneficial owners to comply with the requirements of Circular 37. As a result, we cannot assure you that all of our shareholders or beneficial owners who are PRC residents or entities have complied with, and will in the future make or obtain any applicable registrations or approvals required by, Circular 37 or other PRC applicable law and regulations related to outbound investment. Failure by such shareholders or beneficial owners to comply with Circular 37, or failure by us to amend the foreign exchange registrations of our PRC subsidiaries, could subject us to fines or legal sanctions, restrict our overseas or cross-border investment activities and limit our PRC subsidiaries’ ability to make distributions or pay dividends to us or affect our ownership structure, which could adversely affect our business and prospects.

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Any failure to comply with PRC regulations regarding the registration requirements for employee stock incentive plans may subject the PRC plan participants or us to fines and other legal or administrative sanctions.

Pursuant to the Notices on Issues Concerning the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Publicly-Listed Company, promulgated by SAFE in 2012, or SAFE Notices No. 7, PRC citizens and non-PRC citizens who reside in China for a continuous period of no less than one year who participate in any stock incentive plan of an overseas publicly listed company offered to the director, supervisor, senior management and other employees of, and any individual who has labor relationship with its domestic affiliated entities are required to register with SAFE through a domestic qualified agent, which could be a PRC subsidiary of such overseas listed company, and complete certain other procedures. In addition, an overseas entrusted institution must be retained to handle matters in connection with the exercise or sale of stock options and the purchase or sale of shares and interests. We and our directors, executive officers and other employees who are PRC citizens or who reside in the PRC for a continuous period of no less than one year and who have been granted stock options are subject to these regulations. Failure to complete the SAFE registrations for our employee incentive plans may subject them to fines and legal sanctions, and may also limit our ability to contribute additional capital into our PRC subsidiaries and limit our PRC subsidiaries' ability to distribute dividends to us. We also face regulatory uncertainties that could restrict our ability to adopt additional incentive plans for our directors, executive officers and employees under PRC law.

In addition, the State Taxation Administration of the PRC, or STA, has issued certain circulars concerning employee stock options and restricted shares. Under these circulars, our employees working in China who exercise stock options or are granted restricted shares will be subject to PRC individual income tax. Our PRC subsidiaries have obligations to file documents related to employee stock options or restricted shares with relevant tax authorities and to withhold individual income taxes of those employees who exercise their share options or are granted with restricted shares. If our employees fail to pay or we fail to withhold their income taxes according to relevant laws and regulations, we may face sanctions imposed by the tax authorities or other PRC governmental authorities.

U.S. regulatory bodies may be limited in their ability to conduct investigations or inspections of our operations in China.

Any disclosure of documents or information located in China to foreign agencies may be subject to jurisdiction constraints and must comply with China's state secrecy laws, which broadly define the scope of "state secrets" to include matters involving economic interests and technologies. There is no guarantee that requests from U.S. federal or state regulators or agencies to investigate or inspect our operations will be honored by us, by entities who provide services to us or with whom we associate, without violating PRC legal requirements, especially as those entities are located in China. Furthermore, under the current PRC laws, an on-site inspection of our facilities by any of these regulators may be limited or prohibited.

According to Article 177 of the PRC Securities Law, which became effective in March 2020, no overseas securities regulator is allowed to directly conduct investigation or evidence collection activities within the PRC territory, and, without the consent by the PRC securities regulatory authorities and the other competent government agencies, no entity or individual may provide documents or materials related to securities business to a third party located outside the PRC. In addition, the Data Security Law and the Personal Information Protection Law provide that no entity or individual within the PRC territory may provide any foreign judicial body and law enforcement body with any data or any personal information stored within the PRC territory without the approval of the competent PRC government authority.

In April 2022, the CSRC released a Draft Circular on Strengthening the Confidentiality and Archives Administration Relating to Overseas Issuance and Listing of Securities by Domestic Companies (Draft for Comments), according to which, a domestic company shall obtain approval and making filings with relevant authorities when providing or publicly disclosing, by itself or through the overseas listing entity, any document or material which involves national secrets or institutional work secrets. Investigations, collections of evidence or inspections conducted on the domestic company, securities companies and securities service institutions proposed by overseas securities regulatory authorities and relevant competent departments shall be carried out through cross-border regulatory cooperation mechanism. Reporting to CSRC or relevant competent departments shall be made in advance before the domestic company, securities companies and securities service institutions cooperating with such investigation, inspection or providing documents or materials. Although the authorities in China may establish a regulatory cooperation mechanism with the securities regulatory authorities of another country or region to implement cross-border supervision and administration, such cooperation with the securities regulatory authorities in the U.S. may not be efficient in the absence of mutual and practical cooperation mechanism. While detailed interpretation of or implementation rules under these laws are yet to be promulgated, the inability for an overseas securities regulator to directly conduct investigation or evidence collection activities within China may further increase the difficulties you face in protecting your interests.

If we are classified as a PRC resident enterprise for PRC income tax purposes, such classification could result in unfavorable tax consequences to us and our non-PRC shareholders or ADS holders.

Under the Enterprise Income Tax Law of the PRC, or the EIT Law, and its implementation rules, an enterprise established outside of the PRC with “de facto management body” within the PRC is considered a resident enterprise and will be subject to the enterprise income tax on its global income at the rate of 25%. The implementation rules define the term “de facto management body” as the body that exercises full and substantial control and overall management over the business, productions, personnel, accounts and properties of an enterprise. On April 22, 2009, the STA issued a circular, known as Circular 82, which provides certain specific criteria for determining whether the “de facto management body” of a PRC-controlled enterprise that is incorporated offshore is located in China. According to Circular 82, an offshore incorporated enterprise controlled by a PRC enterprise or a PRC enterprise group will be regarded as a PRC tax resident by virtue of having its “de facto management body” in China and will be subject to PRC enterprise income tax on its global income only if all of the following conditions are met: (i) the primary location of the day-to-day operational management is in the PRC; (ii) decisions relating to the enterprise’s financial and human resource matters are made or are subject to approval by organizations or personnel in the PRC; (iii) the enterprise’s primary assets, accounting books and records, company seals, and board and shareholder resolutions, are located or maintained in the PRC; and (iv) at least 50% of voting board members or senior executives habitually reside in the PRC.

Although this circular only applies to offshore enterprises controlled by PRC enterprises or PRC enterprise groups, not those controlled by PRC individuals or foreigners, the criteria set forth in the circular may reflect the STA’s general position on how the “de facto management body” text should be applied in determining the tax resident status of all offshore enterprises. If the PRC tax authorities determine that we should be classified as a PRC resident enterprise for PRC tax purposes, our global income will be subject to income tax at a uniform rate of 25%, which may have a material adverse effect on our financial condition and results of operations. Notwithstanding the foregoing provision, the EIT Law also provides that, if a PRC resident enterprise directly invests in another PRC resident enterprise, the dividends received by the investing PRC resident enterprise from the invested PRC resident enterprise are exempted from income tax, subject to certain conditions. However, it remains unclear how the PRC tax authorities will interpret the PRC tax resident treatment of an offshore company with indirect ownership interests in PRC resident enterprises through intermediary holding companies.

Moreover, if the PRC tax authorities determine that our company is a PRC resident enterprise for PRC enterprise income tax purposes, gains realized on the sale or other disposal of ADSs or ordinary shares may be subject to PRC tax, at a rate of 10% in the case of non-PRC enterprises, or 20% in the case of non-PRC individuals (in each case, subject to the provisions of any applicable tax treaty), if such gains are deemed to be from PRC sources. Any such tax may reduce the returns on your investment in the ADSs.

We may not be able to obtain certain benefits under the relevant tax treaty on dividends paid by our PRC subsidiaries to us through our Hong Kong subsidiary.

Pursuant to the EIT Law and its implementation rules, if a non-resident enterprise has not set up an organization or establishment in the PRC, or has set up an organization or establishment but the income derived has no actual connection with such organization or establishment, it will be subject to a withholding tax on its PRC-sourced income at a rate of 10%. Pursuant to the Arrangement between Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Tax Evasion on Income, or the Double Taxation Arrangement, the withholding tax rate in respect to the payment of dividends by a PRC enterprise to a Hong Kong enterprise is reduced to 5% from a standard rate of 10% if the Hong Kong enterprise directly holds at least 25% of the PRC enterprise. There are also other conditions for enjoying the reduced withholding tax rate according to other relevant tax rules and regulations.

In February 2009, STA issued STA Notice No. 81, pursuant to which an enterprise must be the “beneficial owner” of the relevant dividend income in order to enjoy the preferential withholding tax rates on dividend. If, however, such enterprise otherwise qualifies for such preferential withholding tax rates through any transaction or arrangement, whose main purpose is to qualify for such preferential withholding tax rates, the enterprise nevertheless cannot enjoy the preferential withholding tax rates and the competent tax authority has the power to adjust the applicable withholding tax rates if it so determines. A STA Notice No. 9 issued by STA that took effect in April 2018 indicated that “beneficial owner” refers to a person who has ownership and disposal rights to the income or any rights and assets arising from such income, and the tax authority has discretion to determine whether or not an enterprise is determined as a “beneficial owner.” However, since the STA Notice No. 9 is newly issued, it remains unclear how the PRC tax authorities will implement STA Notice No. 9 in practice and to what extent they will affect the dividend withholding tax rates for dividends distributed by our PRC subsidiaries to our Hong Kong subsidiary. If the relevant tax authority determines that our Hong Kong subsidiary is a conduit company and does not qualify as the “beneficial owner” of the dividend income it receives from our PRC subsidiaries, the higher 10% withholding tax rate will apply to such dividends.

Entitlement to a lower tax rate on dividends according to tax treaties or arrangements between the PRC central government and governments of other countries or regions is further subject to the Administrative Measures for Non-Resident Taxpayers to Enjoy Treatments under Tax Treaties promulgated by the STA on October 14, 2019 and became effective from January 1, 2020, which provides that non-resident enterprises are not required to obtain pre-approval from the relevant tax authority in order to enjoy the reduced withholding tax. Instead, non-resident enterprises and their withholding agents may, by self-assessment and on confirmation that the prescribed criteria to enjoy the tax treaty benefits are met, directly apply the reduced withholding tax rate, collect and retain relevant materials for reference in accordance with these treaties, and accept supervision and management from the tax authorities. Therefore, we cannot assure you that our determination regarding our qualification to enjoy the preferential tax treatment will not be challenged by the relevant PRC tax authority or we will be able to complete the necessary filings with the relevant PRC tax authority and enjoy the preferential withholding tax rate of 5% under the Double Taxation Arrangement with respect to dividends to be paid by our PRC subsidiaries to Yao Wang Corporation Limited, our Hong Kong subsidiary.

We face uncertainty with respect to indirect transfers of equity interests in PRC resident enterprises by their non-PRC holding companies.

We face uncertainties regarding the reporting on and consequences of previous private equity financing transactions involving the transfer and exchange of shares in our company by non-PRC resident investors.

According to the Notice on Strengthening Administration of Enterprise Income Tax for Share Transfers by Non-PRC Resident Enterprises issued by STA on December 10, 2009, or STA Circular 698, where a non-PRC resident enterprise transfers the equity interests in a PRC resident enterprise indirectly through a disposition of equity interests in an offshore holding company (other than the sale on a public stock market of shares of an offshore enterprise purchased on a public stock market), or an Indirect Transfer, the non-PRC resident enterprise, as the seller, may be subject to PRC enterprise income tax of up to 10% of the gains derived from the Indirect Transfer in certain circumstances.

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On February 3, 2015, the STA issued the Announcement on Several Issues Concerning the Enterprise Income Tax on Indirect Property Transfers by Non-PRC Resident Enterprises, or STA Notice No. 7, to supersede the existing tax rules in relation to the tax treatment of the Indirect Transfer, while the other provisions of STA Circular 698 are irrelevant to the Indirect Transfer remain in force. STA Notice No. 7 introduces a new tax regime that is significantly different from that under a notice issued by STA Circular 698. It extends STA's tax jurisdiction to capture not only the Indirect Transfer as set forth under STA Circular 698 but also transactions involving indirect transfer of (i) real properties in China and (ii) assets of an "establishment or place" situated in China, by a non-PRC resident enterprise through a disposition of equity interests in an offshore holding company. STA Notice No. 7 also extends the interpretation with respect to the disposition of equity interests in an offshore holding company broadly. In addition, STA Notice No. 7 further clarifies how to assess reasonable commercial purposes and introduces safe harbors applicable to internal group restructurings. However, it also brings challenges to both offshore transferor and transferee as they are required to make self-assessments on whether an Indirect Transfer or similar transaction should be subject to PRC tax and whether they should file or withhold any tax payment accordingly. On October 17, 2017, the STA issued a Notice Concerning Withholding Income Tax of Non-Resident Enterprise, or STA Notice No. 37, which abolished STA Circular 698 and certain provisions of STA Notice No. 7 and STA Notice No. 37 further reduced the burden of the withholding obligator, such as revocation of contract filing requirements and tax liquidation procedures, strengthened the cooperation of tax authorities in different places, and clarified the calculation of tax payable and mechanism of foreign exchange.

There is uncertainty as to the application of STA Notice No. 7 and STA Notice No. 37. In the event that non-PRC resident investors were involved in our private equity financing transactions and such transactions were determined by the competent tax authorities as lacking reasonable commercial purposes, we and our non-PRC resident investors may become at risk of being taxed under and STA Notice No. 7 and STA Notice No. 37 and may be required to expend costly resources to comply with STA Notice No. 7 and STA Notice No. 37, or to establish a case to be tax exempt under STA Notice No. 7 and STA Notice No. 37, which may cause us to incur additional costs and may have a negative impact on the value of your investment in us.

The PRC tax authorities have discretion under STA Notice No. 7 and STA Notice No. 37 to adjust the taxable capital gains based on the difference between the fair value of the transferred equity interests and the investment cost. We may pursue acquisitions in the future that may involve complex corporate structures. If we are deemed as a non-PRC resident enterprise under the EIT Law and if the PRC tax authorities adjust the taxable income of the transactions under STA Notice No. 7 and STA Notice No. 37, our income tax expenses associated with such potential acquisitions will increase, which may have an adverse effect on our financial condition and results of operations.

The PCAOB is currently unable to inspect our auditor in relation to their audit work performed for our financial statements and the inability of the PCAOB to conduct inspections over our auditor deprives our investors with the benefits of such inspections.

Our auditor, the independent registered public accounting firm that issues the audit report included elsewhere in this annual report, as an auditor of companies that are traded publicly in the United States and a firm registered with the Public Company Accounting Oversight Board (United States), or the PCAOB, is subject to laws in the United States pursuant to which the PCAOB conducts regular inspections to assess its compliance with the applicable professional standards. Since our auditor is located in China, a jurisdiction where the PCAOB has been unable to conduct inspections without the approval of the Chinese authorities, our auditor is not currently inspected by the PCAOB. This lack of the PCAOB inspections in China prevents the PCAOB from fully evaluating audits and quality control procedures of our independent registered public accounting firm. As a result, we and investors in our ordinary shares are deprived of the benefits of such PCAOB inspections. The inability of the PCAOB to conduct inspections of auditors in China makes it more difficult to evaluate the effectiveness of our independent registered public accounting firm's audit procedures or quality control procedures as compared to auditors outside of China that are subject to the PCAOB inspections, which could cause investors and potential investors in our stock to lose confidence in our audit procedures and reported financial information and the quality of our financial statements.

Our ADSs may be delisted and our ADSs and Class A ordinary shares may be prohibited from trading in the over-the-counter market under the Holding Foreign Companies Accountable Act, or the HFCAA, if the PCAOB is unable to inspect or fully investigate auditors located in China. On December 16, 2021, PCAOB issued the HFCAA Determination Report, according to which our auditor is subject to the determinations that the PCAOB is unable to inspect or investigate completely. Under the current law, delisting and prohibition from over-the-counter trading in the U.S. could take place in 2024. If this happens there is no certainty that we will be able to list our ADSs or Class A ordinary shares on a non-U.S. exchange or that a market for our ADSs or Class A ordinary shares will develop outside of the U.S. The delisting of our ADSs, or the threat of their being delisted, may materially and adversely affect the value of your investment.

As part of a continued regulatory focus in the United States on access to audit and other information currently protected by national law, in particular China's, the Holding Foreign Companies Accountable Act, or the HFCAA has been signed into law on December 18, 2020. The HFCAA states if the SEC determines that we have filed audit reports issued by a registered public accounting firm that has not been subject to inspection for the PCAOB for three consecutive years beginning in 2021, the SEC shall prohibit our Class A ordinary shares or ADSs from being traded on a national securities exchange or in the over-the-counter trading market in the U.S. Accordingly, under the current law this could happen in 2024.

On December 2, 2021, the SEC adopted final amendments to its rules implementing the HFCAA (the "Final Amendments"). The Final Amendments include requirements to disclose information, including the auditor name and location, the percentage of shares of the issuer owned by governmental entities, whether governmental entities in the applicable foreign jurisdiction with respect to the auditor has a controlling financial interest with respect to the issuer, the name of each official of the Chinese Communist Party who is a member of the board of the issuer, and whether the articles of incorporation of the issuer contains any charter of the Chinese Communist Party. The Final Amendments also establish procedures the SEC will follow in identifying issuers and prohibiting trading by certain issuers under the HFCAA.

On December 16, 2021, PCAOB issued the HFCAA Determination Report, according to which our auditor is subject to the determinations that the PCAOB is unable to inspect or investigate completely. The HFCAA or other efforts to increase U.S. regulatory access to audit information could cause investor uncertainty for affected issuers, including us, and the market price of the ADSs could be adversely affected.

In March 2022, the SEC issued its first "Conclusive list of issuers identified under the HFCAA" indicating that those companies are now formally subject to the delisting provisions if they remain on the list for three consecutive years. We anticipate being added to the list shortly after the filing of this annual report. Additionally, whether the PCAOB will be able to conduct inspections of our auditor before the issuance of our financial statements on Form 20-F for the year ended December 31, 2023, which is due by April 30, 2024, or at all, is subject to substantial uncertainty and depends on factors out of our and our auditor's control. If our auditor is unable to be inspected in time, we could be delisted from the NASDAQ and our ADSs will not be permitted for trading "over-the-counter" either. Such a delisting would substantially impair your ability to sell or purchase our ADSs when you wish to do so, and the risk and uncertainty associated with delisting would have a negative impact on the price of our ADSs. Also, such a delisting would significantly affect our ability to raise capital on terms acceptable to us, or at all, which would have a material adverse impact on our business, financial condition, and prospects. If our shares and ADSs are prohibited from trading in the United States, there is no certainty that we will be able to list on a non-U.S. exchange or that a market for our shares will develop outside of the United States. Such a prohibition would substantially impair your ability to sell or purchase our ADSs when you wish to do so, and the risk and uncertainty associated with delisting would have a negative impact on the price of our ADSs. In addition, such a prohibition would significantly affect our ability to raise capital on terms acceptable to us, or at all, which would materially and adversely affect our business, financial condition, and prospects.

The potential enactment of the Accelerating Holding Foreign Companies Accountable Act would decrease the number of non-inspection years from three years to two, thus reducing the time period before our ADSs may be prohibited from over-the-counter trading or delisted. If this bill were enacted, our ADS could be delisted from the exchange and prohibited from over-the-counter trading in the U.S. in 2023.

On June 22, 2021, the U.S. Senate passed the Accelerating Holding Foreign Companies Accountable Act, or the AHFCA Act, which, if enacted into law, would amend the HFCAA and require the SEC to prohibit an issuer's securities from trading on any U.S. stock exchanges if its auditor is not subject to PCAOB inspections for two consecutive years, instead of three consecutive years as currently enacted in the HFCAA.

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On February 4, 2022, the U.S. House of Representatives passed the America Competes Act of 2022 which includes the exact same amendments as the bill passed by the Senate. The America Competes Act however includes a broader range of legislation not related to the HFCAA in response to the U.S. Innovation and Competition Act passed by the Senate in 2021. The U.S. House of Representatives and U.S. Senate will need to agree on amendments to these respective bills to align the legislation and pass their amended bills before the President can sign into law. It is unclear when the U.S. Senate and U.S. House of Representatives will resolve the differences in the U.S. Innovation and Competition Act and the America Competes Act of 2022 bills currently passed, or when the U.S. President will sign on the bill to make the amendment into law, or at all.

In the case that the bill becomes the law, it will reduce the time period before our ADSs could be delisted from the exchange and prohibited from over-the-counter trading in the U.S. from 2024 to 2023.

Proceedings instituted by the SEC against Chinese affiliates of the “big four” accounting firms, including our independent registered public accounting firm, could result in financial statements being determined to not be in compliance with the requirements of the Exchange Act.

In December 2012, the SEC instituted administrative proceedings against the Big Four PRC-based accounting firms, including our independent registered public accounting firm, alleging that these firms had violated U.S. securities laws and the SEC’s rules and regulations thereunder by failing to provide to the SEC the firms’ audit work papers with respect to certain PRC-based companies that are publicly traded in the United States.

On January 22, 2014, the administrative law judge presiding over the matter rendered an initial decision that each of the firms had violated the SEC’s rules of practice by failing to produce audit papers and other documents to the SEC. The initial decision censured each of the firms and barred them from practicing before the SEC for a period of six months.

On February 6, 2015, the four China-based accounting firms each agreed to a censure and to pay a fine to the SEC to settle the dispute and avoid suspension of their ability to practice before the SEC and audit U.S.-listed companies. The settlement required the firms to follow detailed procedures and to seek to provide the SEC with access to Chinese firms’ audit documents via the CSRC. Under the terms of the settlement, the underlying proceeding against the four China-based accounting firms was deemed dismissed with prejudice four years after entry of the settlement. The four-year mark occurred on February 6, 2019. While we cannot predict if the SEC will further challenge the four China-based accounting firms’ compliance with U.S. law in connection with U.S. regulatory requests for audit work papers or if the results of such a challenge would result in the SEC imposing penalties such as suspensions, if the accounting firms are subject to additional remedial measures, our ability to file our financial statements in compliance with SEC requirements could be impacted. A determination that we have not timely filed financial statements in compliance with the SEC requirements could ultimately lead to the delisting of our ADSs from the Nasdaq or the termination of the registration of our ordinary shares under the Securities Exchange Act of 1934, or both, which would substantially reduce or effectively terminate the trading of our ADSs in the United States.

Risks Related to American Depository Shares

The trading price for the ADSs may be volatile.

Since the ADSs became listed on Nasdaq on September 12, 2018, the trading price of the ADSs has ranged from US\$1.63 to US\$45.88. The trading prices of the ADSs are likely to be volatile and could fluctuate widely due to factors beyond our control. This may happen because of broad market and industry factors, like the performance and fluctuation in the trading prices or the underperformance or deteriorating financial results of internet or other companies based in China that have listed their securities in the United States in recent years. The securities of some of these companies have experienced significant volatility since their initial public offerings, including, in some cases, substantial price declines in their trading prices. The trading performances of other Chinese companies’ securities after their offerings, including internet and e-commerce companies, may affect the attitudes of investors toward Chinese companies listed in the United States, which consequently may impact the trading performance of the ADSs, regardless of our actual operating performance. In addition, any negative news or perceptions about inadequate corporate governance practices or fraudulent accounting, corporate structure or other matters of other Chinese companies may also negatively affect the attitudes of investors towards Chinese companies in general, including us, regardless of whether we have conducted any inappropriate activities. In addition, securities markets may from time to time experience significant price and volume fluctuations that are not related to our operating performance, which may have a material adverse effect on the trading price of the ADSs.

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In addition to the above factors, the price and trading volume of the ADSs may be highly volatile due to multiple factors, including the following:

- regulatory developments affecting us, our consumers or our industry;
- conditions in the online healthcare industry and the public perception of the legitimacy and ethics of certain business practices of our competitors or other market players within the industry;
- announcements of studies and reports relating to the quality of our product and service offerings or those of our competitors;
- changes in the economic performance or market valuations of other online healthcare platforms;
- actual or anticipated fluctuations in our quarterly results of operations and changes or revisions of our expected results;
- changes in financial estimates by securities research analysts;
- announcements by us or our competitors of new product and service offerings, acquisitions, strategic relationships, joint ventures or capital commitments;
- additions to or departures of our senior management;
- detrimental negative publicity about us, our management or our industry;
- the potential delisting pursuant to the HFCAA;
- fluctuations of exchange rates between the Renminbi and the U.S. dollar;
- allegations of a lack of effective internal control over financial reporting resulting in financial and accounting irregularities and mistakes; inadequate corporate governance policies, or allegations of fraud, among other things, involving China-based issuers;
- release or expiry of any transfer restrictions on our outstanding ordinary shares or the ADSs; and
- sales or perceived potential sales of additional ordinary shares or ADSs.

The trading market for the ADSs will depend in part on the research and reports that securities or industry analysts publish about us or our business. If research analysts do not establish and maintain adequate research coverage or if one or more of the analysts who cover us downgrade the ADSs or publish inaccurate or unfavorable research about our business, the trading price for our ADSs would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, we could lose visibility in the financial markets, which, in turn, could cause the trading price or trading volume for the ADSs to decline.

Techniques employed by short sellers may drive down the trading price of the ADSs.

Short selling is the practice of selling securities that the seller does not own but rather has borrowed from a third party with the intention of buying identical securities back at a later date to return to the lender. The short seller hopes to profit from a decline in the value of the securities between the sale of the borrowed securities and the purchase of the replacement shares, as the short seller expects to pay less in that purchase than it received in the sale. As it is in the short seller's interest for the price of the security to decline, many short sellers publish, or arrange for the publication of, negative opinions regarding the relevant issuer and its business prospects in order to create negative market momentum and generate profits for themselves after selling a security short. These short attacks have, in the past, led to selling of shares in the market.

Public companies that have substantially all of their operations in China have been the subject of short selling. Most of the scrutiny and negative publicity raised in the short seller reports has centered on allegations of a lack of effective internal control over financial reporting resulting in financial and accounting irregularities and mistakes, inadequate or ineffective disclosure controls and

procedures or a lack of adherence thereto, related party transactions at the cost of the public investors, and, in many cases, allegations of fraud. As a result, many of these companies are now conducting internal and external investigations into the allegations and, in the interim, are subject to shareholder lawsuits or enforcement actions by the SEC, Department of Justice and other U.S. regulatory authorities.

It is not clear what effect such negative publicity could have on us. If we were to become the subject of any unfavorable allegations, whether such allegations are proven to be true or untrue, we could have to expend a significant amount of resources to investigate such allegations or defend ourselves in shareholder litigation or regulatory enforcement actions. While we would strongly defend against any such short seller attacks, we may be constrained in the manner in which we can proceed against the relevant short seller by principles of freedom of speech, applicable state law or issues of commercial confidentiality. Such a situation could be costly and time-consuming, and could distract our management from growing our business. Even if such allegations are ultimately proven to be groundless, allegations against us could severely impact our business operations, and any investment in the ADSs could be greatly reduced or even rendered worthless.

Our dual-class share structure with different voting rights will limit your ability to influence corporate matters and could discourage others from pursuing any change of control transactions that holders of our Class A ordinary shares and ADSs may view as beneficial.

We have a dual-class share structure such that our ordinary shares consists of Class A ordinary shares and Class B ordinary shares. In respect of matters requiring the votes of shareholders, holders of Class A ordinary shares will be entitled to one vote per share, while holders of Class B ordinary shares will be entitled to fifteen votes per share based on our dual-class share structure. Each Class B ordinary share is convertible into one Class A ordinary share at any time by the holder thereof, while Class A ordinary shares are not convertible into Class B ordinary shares under any circumstances. Upon any sale, transfer, assignment or disposition of any Class B ordinary share by our Founders (defined in our memorandum and articles of association to mean Dr. Gang Yu and Mr. Junling Liu) or Founder Affiliate (as defined in our memorandum and articles of association) to any person who is not a “Founder Affiliate,” or upon a change of ultimate beneficial ownership of any Class B ordinary share to any person who is not a Founder Affiliate, such Class B ordinary share shall be automatically and immediately converted into one Class A ordinary share.

As of March 31, 2022, our founders, Dr. Gang Yu and Mr. Junling Liu, beneficially own all of our issued and outstanding Class B ordinary shares. These Class B ordinary shares constitute approximately 43.2% of our total outstanding share capital and 92.0% of the aggregate voting power of our total outstanding share capital due to the disparate voting powers associated with our dual-class share structure. See “Item 6. Directors, Senior Management and Employees—E. Share Ownership.” As a result of the dual-class share structure and the concentration of ownership, holders of Class B ordinary shares will have considerable influence over matters such as decisions regarding mergers, consolidations and the sale of all or substantially all of our assets, election of directors and other significant corporate actions. Such holders may take actions that are not in the best interest of us or our other shareholders. This concentration of ownership may discourage, delay or prevent a change in control of our company, which could have the effect of depriving our other shareholders of the opportunity to receive a premium for their shares as part of a sale of our company and may reduce the price of our ADSs. This concentrated control will limit your ability to influence corporate matters and could discourage others from pursuing any potential merger, takeover or other change of control transactions that holders of Class A ordinary shares and ADSs may view as beneficial.

The dual-class structure of our ordinary shares may adversely affect the trading market for our ADSs.

S&P Dow Jones and FTSE Russell have recently announced changes to their eligibility criteria for inclusion of shares of public companies on certain indices, including the S&P 500, to exclude companies with multiple classes of shares and companies whose public shareholders hold no more than 5% of total voting power from being added to such indices. In addition, several shareholder advisory firms have announced their opposition to the use of multiple class structures. As a result, the dual-class structure of our ordinary shares may prevent the inclusion of our ADSs representing Class A ordinary shares in such indices and may cause shareholder advisory firms to publish negative commentary about our corporate governance practices or otherwise seek to cause us to change our capital structure. Any such exclusion from indices could result in a less active trading market for our ADSs. Any actions or publications by shareholder advisory firms critical of our corporate governance practices or capital structure could also adversely affect the value of our ADSs.

Because we do not expect to pay dividends in the foreseeable future, you must rely on price appreciation of the ADSs for return on your investment.

We currently intend to retain most, if not all, of our available funds and any future earnings to fund the development and growth of our business. As a result, we do not expect to pay any cash dividends in the foreseeable future. Therefore, you should not rely on an investment in the ADSs as a source for any future dividend income.

Our board of directors has discretion as to whether to distribute dividends, subject to certain restrictions under Cayman Islands law, namely that our company may only pay dividends out of profits or share premium account; provided that in no circumstances may a dividend be paid if this would result in our company being unable to pay its debts as they fall due in the ordinary course of business. In addition, our shareholders may by ordinary resolution declare a dividend, but no dividend may exceed the amount recommended by our board of directors. Even if our board of directors decides to declare and pay dividends, the timing, amount and form of future dividends, if any, will depend on, among other things, our future results of operations and cash flow, our capital requirements and surplus, the amount of distributions, if any, received by us from our subsidiaries, our financial condition, contractual restrictions and other factors deemed relevant by our board of directors. Accordingly, the return on your investment in our ADSs will likely depend entirely upon any future price appreciation of our ADSs. There is no guarantee that our ADSs will appreciate in value in the future or even maintain the price at which you purchased the ADSs. You may not realize a return on your investment in our ADSs and you may even lose your entire investment in our ADSs.

Substantial future sales or perceived potential sales of ADSs in the public market could cause the price of the ADSs to decline.

Sales of ADSs in the public market, or the perception that these sales could occur, could cause the trading price of the ADSs to decline. As of March 31, 2022, we have 166,543,166 ordinary shares outstanding, including 94,543,166 Class A ordinary shares. All of our ADSs are freely transferable without restriction or additional registration under the Securities Act of 1933, as amended, or the Securities Act. The remaining Class A ordinary shares will be available for sale subject to volume and other restrictions as applicable under Rules 144 and 701 under the Securities Act.

Certain holders of our Class A ordinary shares may cause us to register, under the Securities Act, the sale of their shares. Registration of these shares under the Securities Act would result in ADSs representing these shares becoming freely tradable without restriction under the Securities Act immediately upon the effectiveness of the registration. Sales of ADSs representing these registered shares in the public market could cause the price of the ADSs to decline.

The voting rights of holders of ADSs are limited by the terms of the deposit agreement, and you may not be able to exercise your right to direct the voting of the underlying Class A ordinary shares which are represented by your ADSs.

As a Cayman Islands exempted company, we are not obliged by the Companies Act (As Revised) of the Cayman Islands to call shareholders' annual general meetings. As a holder of ADSs, you will not have any direct right to attend general meetings of our shareholders or to cast any votes at such meetings. You will only be able to exercise the voting rights that attach to the underlying Class A ordinary shares represented by your ADSs indirectly by giving voting instructions to the depositary in accordance with the provisions of the deposit agreement. Under the deposit agreement, you may vote only by giving voting instructions to the depositary, as the holder of the underlying Class A ordinary shares that are represented by your ADSs. If we ask the depositary to solicit your instructions, upon receipt of your voting instructions, the depositary will endeavor to vote the underlying Class A ordinary shares in accordance with your instructions. If we do not instruct the depositary to solicit, you can still send voting instructions to the depositary, and the depositary may, but is not required, to endeavor to carry out those instructions. You will not be able to directly exercise any right to vote with respect to the underlying Class A ordinary shares unless you withdraw the shares and become the registered holder of such shares prior to the record date for the general meeting. Under our memorandum and articles of association, the minimum notice period required to be given by our company to our registered shareholders for convening a general meeting is ten calendar days. When a general meeting is convened, you may not receive sufficient advance notice to enable you to withdraw the underlying shares which are represented by your ADSs and become the registered holder of such shares prior to the record date for the general meeting to allow you to attend the general meeting or to vote directly with respect to any specific matter or resolution which is to be considered and voted upon at the general meeting. In addition, under our memorandum and articles of association, for the purposes of determining those shareholders who are entitled to attend and vote at any general meeting, our directors may close our register of members and/or fix in advance a record date for such meeting, and such closure of our register of members or the setting of such a record date may prevent you from withdrawing the underlying shares which are represented by your ADSs and becoming the registered holder of such shares prior to the record date, so that you would not be able to attend the general meeting or to vote directly.

Where any matter is to be put to a vote at a general meeting, the depositary will endeavor to notify you of the upcoming vote and to deliver our voting materials to you if we ask it to. We cannot assure you that you will receive the voting materials in time to ensure that you can instruct the depositary to vote the underlying shares which are represented by your ADSs. In addition, the depositary and its agents are not responsible for failing to carry out voting instructions or for their manner of carrying out your voting instructions. This means that you may not be able to exercise your right to direct the voting of the underlying shares that are represented by your ADSs, and you may have no legal remedy if the underlying shares are not voted as you requested.

The depositary for our ADSs may give us a discretionary proxy to vote the Class A ordinary shares underlying your ADSs if you do not give voting instructions, which could adversely affect your interests.

Under the deposit agreement for the ADSs, if (i) we timely instruct the depositary to solicit your voting instructions, the depositary does not receive your instructions by the specified date and (ii) we confirm to the depositary that:

- we wish a discretionary proxy to be given;
- we reasonably believe there is no substantial opposition as to a matter to be voted on at the meeting; and
- a matter to be voted on at the meeting would not have a material adverse impact on shareholders,

then the depositary will give us a proxy to vote the shares represented by your ADSs. The effect of this discretionary proxy is that, if you fail to give voting instructions to the depositary as to how to vote the Class A ordinary shares underlying your ADSs at any particular shareholders' meeting, you cannot prevent our ordinary shares underlying your ADSs from being voted at that meeting, and it may make it more difficult for shareholders to influence our management. Holders of our Class A ordinary shares are not subject to this discretionary proxy.

The deposit agreement may be amended or terminated without your consent.

We and the depositary may amend the deposit agreement, and we may initiate termination of it, without your consent. If you continue to hold your ADSs after an amendment to the deposit agreement, you agree to be bound by the deposit agreement as amended. See "Item 12. Description of Securities Other Than Equity Securities—Description of American Depository Shares" for more information.

Your right to participate in any future rights offerings may be limited, which may cause dilution of your holdings.

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. However, we cannot make such rights available to you in the United States unless we register the securities to which the rights relate under the Securities Act or an exemption from the registration requirements is available. Under the deposit agreement, the depositary will not make rights available to you unless the underlying securities to be distributed to ADS holders are either registered under the Securities Act or exempt from registration under the Securities Act. We are under no obligation to file a registration statement with respect to any such rights or securities or to endeavor to cause such a registration statement to be declared effective and we may not be able to establish a necessary exemption from registration under the Securities Act. Accordingly, you may be unable to participate in our rights offerings in the future and may experience dilution in your holdings.

You may not receive dividends or other distributions on our Class A ordinary shares and you may not receive any value for them, if it is illegal or impractical to make them available to you.

The depositary has agreed to pay to you the cash dividends or other distributions it or the custodian receives on our Class A ordinary shares or other deposited securities underlying our ADSs, after deducting its fees and expenses. You will receive these distributions in proportion to the number of Class A ordinary shares your ADSs represent. However, the depositary is not responsible if it decides that it is unlawful or impractical to make a distribution available to any holders of ADSs. For example, it would be unlawful to make a distribution to a holder of ADSs if it consists of securities that require registration under the Securities Act but that are not properly registered or distributed under an applicable exemption from registration. The depositary may also determine that it is not feasible to distribute certain property through the mail. Additionally, the value of certain distributions may be less than the cost of mailing them. In these cases, the depositary may determine not to distribute such property. We have no obligation to register under U.S. securities laws any ADSs, ordinary shares, rights or other securities received through such distributions. We also have no

obligation to take any other action to permit the distribution of ADSs, ordinary shares, rights or anything else to holders of ADSs. This means that you may not receive distributions we make on our Class A ordinary shares or any value for them if it is illegal or impractical for us to make them available to you. These restrictions may cause a material decline in the value of the ADSs.

Holders of ADS may experience difficulties in effecting service of legal process, enforcing foreign, including U.S., judgments or bringing actions in China against us or our directors and management named in this offering memorandum based on foreign laws, including U.S. securities law.

We are an exempted company limited by shares incorporated under the laws of the Cayman Islands. We conduct substantially all of our operations in China and substantially all of our assets are located in China. In addition, a majority of our directors and executive officers reside within China, and most of the assets of these persons are located within China. As a result, it may be difficult or impossible for you to effect service of process within the United States upon these individuals, or to bring an action against us or against these individuals in the United States in the event that you believe your rights have been infringed under the U.S. federal securities laws or otherwise. Even if you are successful in bringing an action of this kind, the laws of the Cayman Islands and of the PRC may render you unable to enforce a judgment against our assets or the assets of our directors and officers. However, the deposit agreement gives you the right to submit claims against us to binding arbitration, and arbitration awards may be enforceable against us and our assets in China even when court judgments are not.

Shareholder claims that are common in the United States, including securities law class actions and fraud claims, generally are difficult to pursue as a matter of law or practicality in China. In particular, in China, there are significant legal, regulatory and other obstacles to obtaining information needed for shareholder investigations or litigation outside China or otherwise involving foreign persons or entities as plaintiffs. Although the local authorities in China may establish a regulatory cooperation mechanism with the securities regulatory authorities of foreign jurisdictions to implement cross-border supervision and litigation, such regulatory cooperation with the securities regulatory authorities in the United States have not been efficient in the absence of mutual and practical implementation mechanism. Under the PRC Securities Law, no PRC entity or individual may provide the documents and materials relating to securities trading and market activities to overseas parties without prior consent of the competent securities regulatory authority in China.

You may face difficulties in protecting your interests, and your ability to protect your rights through U.S. courts may be limited, because we are incorporated under Cayman Islands law.

We are an exempted company limited by shares incorporated under the laws of the Cayman Islands. Our corporate affairs are governed by our memorandum and articles of association, the Companies Act (As Revised) of the Cayman Islands and the common law of the Cayman Islands. The rights of shareholders to take action against our directors, actions by our minority shareholders and the fiduciary duties of our directors to us under Cayman Islands law are to a large extent governed by the common law of the Cayman Islands. The common law of the Cayman Islands is derived in part from comparatively limited judicial precedent in the Cayman Islands as well as from the common law of England, the decisions of whose courts are of persuasive authority, but are not binding, on a court in the Cayman Islands. The rights of our shareholders and the fiduciary duties of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedent in some jurisdictions in the United States. In particular, the Cayman Islands has a less developed body of securities laws than the United States. Some U.S. states, such as Delaware, have more fully developed and judicially interpreted bodies of corporate law than the Cayman Islands. In addition, Cayman Islands companies may not have standing to initiate a shareholder derivative action in a federal court of the United States.

Shareholders of Cayman Islands exempted companies like us have no general rights under Cayman Islands law to inspect corporate records (other than copies of our memorandum and articles of association, register of mortgages and charges, and any special resolutions passed by our shareholders) or to obtain copies of lists of shareholders of these companies. Our directors will have discretion under our memorandum and articles of association to determine whether or not, and under what conditions, our corporate records may be inspected by our shareholders, but are not obliged to make them available to our shareholders. This may make it more difficult for you to obtain the information needed to establish any facts necessary for a shareholder resolution or to solicit proxies from other shareholders in connection with a proxy contest.

As a result of all of the above, our public shareholders may have more difficulty in protecting their interests in the face of actions taken by our management, members of the board of directors or controlling shareholders than they would as public shareholders of a company incorporated in the United States.

We may need additional capital and may sell additional ADSs or other equity securities or incur indebtedness, which could result in additional dilution to our shareholders or increase our debt service obligations.

We may require additional cash resources due to changed business conditions or other future developments, including any investments or acquisitions we may decide to pursue. If our cash resources are insufficient to satisfy our cash requirements, we may seek to sell additional equity or debt securities or obtain a credit facility. The sale of additional equity securities or equity-linked debt securities could result in additional dilution to our shareholders. The incurrence of indebtedness would result in debt service obligations and could result in operating and financing covenants that would restrict our operations. We cannot assure you that financing will be available in amounts or terms acceptable to us, if at all.

Our memorandum and articles of association contains anti-takeover provisions that could discourage a third party from acquiring us and adversely affect the rights of holders of our Class A ordinary shares and the ADSs.

Our memorandum and articles of association contains certain provisions that could limit the ability of others to acquire control of our company, including a provision that grants authority to our board of directors to establish and issue from time to time one or more series of preferred shares without action by our shareholders and to determine, with respect to any series of preferred shares, the terms and rights of that series. These provisions could have the effect of depriving our shareholders and holders of the ADSs of the opportunity to sell their shares or ADSs at a premium over the prevailing trading price by discouraging third parties from seeking to obtain control of our company in a tender offer or similar transactions. In addition, our dual-class structure could discourage others from pursuing any change of control transactions. See “—Our dual-class share structure with different voting rights will limit your ability to influence corporate matters and could discourage others from pursuing any change of control transactions that holders of our Class A ordinary shares and the ADSs may view as beneficial.”

Certain existing shareholders have substantial influence over our company and their interests may not be aligned with the interests of our other shareholders.

As of March 31, 2022, our directors and officers collectively owned an aggregate of 92.0% of the total voting power of our outstanding ordinary shares. As a result, they have substantial influence over our business, including significant corporate actions such as mergers, consolidations, election of directors and other significant corporate actions.

They may take actions that are not in the best interest of us or our other shareholders. This concentration of ownership may discourage, delay or prevent a change in control of our company, which could deprive our shareholders of an opportunity to receive a premium for their shares as part of a sale of our company and may reduce the price of the ADSs. These actions may be taken even if they are opposed by our other shareholders. In addition, the significant concentration of share ownership may adversely affect the trading price of the ADSs due to investors’ perception that conflicts of interest may exist or arise. For more information regarding our principal shareholders and their affiliated entities, see “Item 6. Directors, Senior Management and Employees—E. Share Ownership.”

We have granted, and may continue to grant, share incentive awards, which may result in increased share-based compensation expenses.

We adopted our 2016 share incentive plan, or the 2016 Plan, in 2016 to promote our success and the interests of our shareholders by providing a means through which we may grant equity-based incentives to attract, motivate, retain and reward certain officers, employees, directors, consultants and other eligible persons and to further link the interests of recipients with those of our shareholders generally. We adopted certain share incentive policies in December 2013 and August 2014, or the 2013 Policy and the 2014 Policy, respectively. Since the adoption of the 2016 Plan, we stopped granting awards under the 2013 Policy or the 2014 Policy, although the outstanding awards under the 2013 Policy and the 2014 Policy are still being administered under their respective policies. In August 2018, we adopted our 2018 Share Incentive Plan, or the 2018 Plan, which replaced the 2016 Plan in its entirety. Upon the effectiveness of the 2018 Plan, we no longer grant any awards under the 2016 Plan. Outstanding awards granted under the 2016 Plan will remain effective and be subject to the terms and conditions of the 2018 Plan. Under the 2016 Plan, we were authorized to grant options to purchase ordinary shares of our company. The maximum number of ordinary shares which may be issued pursuant to all awards under the 2013 Policy, the 2014 Policy and the 2016 Plan is 13,671,109. Under the 2018 Plan, the maximum number of our shares that may be issued pursuant to all awards is 13,671,109, plus an annual increase on the first day of each fiscal year during the ten-year term of the 2018 Plan commencing with the fiscal year beginning January 1, 2019, by an amount equal to the lesser of (i) 1.0% of the total number of shares issued and outstanding on the last day of the immediately preceding fiscal year, and (ii) such number of shares as may be determined by our board of directors. As of the date of this annual report, options to purchase 7,212,287

Class A ordinary shares and 60,000 restricted share units are granted and outstanding under the 2013 Policy, the 2014 Policy and the 2016 Plan, and options to purchase 2,232,198 Class A ordinary shares and 4,175,604 restricted share units are granted and outstanding under the 2018 Plan. We recognized share-based compensation expenses in the amount of RMB54.3 million, RMB75.7 million and RMB145.6 million (US\$22.8 million) in 2019, 2020 and 2021, respectively. See “Item 6. Directors, Senior Management and Employees —B. Compensation.” We believe the granting of share-based compensation is of significant importance to our ability to attract, retain and incentivize key personnel and employees, and we will continue to grant share-based compensation to employees in the future. As a result, our expenses associated with share-based compensation may increase, which may have an adverse effect on our results of operations.

We are a foreign private issuer within the meaning of the rules under the Exchange Act, and as such we are exempt from certain provisions applicable to U.S. domestic public companies.

Because we qualify as a foreign private issuer under the Exchange Act, we are exempt from certain provisions of the securities rules and regulations in the United States that are applicable to U.S. domestic issuers, including:

- the rules under the Exchange Act requiring the filing with the SEC of quarterly reports on Form 10-Q or current reports on Form 8-K;
- the sections of the Exchange Act regulating the solicitation of proxies, consents or authorizations in respect of a security registered under the Exchange Act;
- the sections of the Exchange Act requiring insiders to file public reports of their stock ownership and trading activities and liability for insiders who profit from trades made in a short period of time; and
- the selective disclosure rules by issuers of material nonpublic information under Regulation FD.

We are required to file an annual report on Form 20-F within four months of the end of each fiscal year. In addition, we intend to publish our results on a quarterly basis as press releases, distributed pursuant to the rules and regulations of the Nasdaq Global Market. Press releases relating to financial results and material events will also be furnished to the SEC on Form 6-K. However, the information we are required to file with or furnish to the SEC will be less extensive and less timely compared to that required to be filed with the SEC by U.S. domestic issuers. As a result, you may not be afforded the same protections or information that would be made available to you were you investing in a U.S. domestic issuer.

As a company incorporated in the Cayman Islands, we are permitted to adopt certain home country practices in relation to corporate governance matters that differ significantly from the Nasdaq Global Market corporate governance requirements; these practices may afford less protection to shareholders than they would enjoy if we complied fully with the Nasdaq Global Market corporate governance requirements.

We may lose our foreign private issuer status in the future, which could result in significant additional costs and expenses.

As discussed above, we are a foreign private issuer, and therefore, we are not required to comply with all of the periodic disclosure and current reporting requirements of the Exchange Act. The determination of foreign private issuer status is made annually on the last business day of an issuer’s most recently completed second fiscal quarter. We would lose our foreign private issuer status if, for example, more than 50% of our ordinary shares are directly or indirectly held by residents of the U.S. and we fail to meet additional requirements necessary to maintain our foreign private issuer status. In the future, if we lose our foreign private issuer status as of the last date of our second fiscal quarter, we would be required to file with the SEC periodic reports and registration statements on U.S. domestic issuer forms beginning on the following January 1, which are more detailed and extensive than the forms available to a foreign private issuer. We would also have to mandatorily comply with U.S. federal proxy requirements, and our officers, directors and principal shareholders would become subject to the short-swing profit disclosure and recovery provisions of Section 16 of the Exchange Act. In addition, we would lose our ability to rely upon exemptions from certain corporate governance requirements under the Nasdaq Global Market listing rules. As a U.S. listed public company that is not a foreign private issuer, we would incur significant additional legal, accounting and other expenses that we will not incur as a foreign private issuer, and accounting, reporting and other expenses in order to maintain a listing on a U.S. securities exchange.

There can be no assurance that we will not be a passive foreign investment company, or PFIC, for any taxable year, which could result in adverse U.S. federal income tax consequences to U.S. investors in the ADSs or ordinary shares.

In general, a non-U.S. corporation is a passive foreign investment company for U.S. federal income tax purposes, or PFIC, for any taxable year in which (i) 75% or more of its gross income consists of passive income; or (ii) 50% or more of the value of its assets (generally determined on an average quarterly basis) consists of assets that produce, or are held for the production of, passive income. For purposes of the above calculations, a non-U.S. corporation that owns (or is treated as owning for U.S. federal income tax purposes), directly or indirectly, at least 25% by value of the shares of another corporation is treated as if it held its proportionate share of the assets of the other corporation and received directly its proportionate share of the income of the other corporation. Passive income generally includes dividends, interest, rents, royalties and certain gains. Cash is generally a passive asset for these purposes. Goodwill (the value of which generally may be determined by reference to the excess of the sum of the corporation's market capitalization and liabilities over the value of its assets) is generally characterized as a non-passive or passive asset based on the nature of the income produced in the activity to which the goodwill is attributable.

Based on the composition of our income and assets and the estimated value of our assets, including goodwill, which is based on the price of our ADSs, we believe that we were not a PFIC for our taxable year ended on December 31, 2021. However, our PFIC status for any taxable year will depend on the composition of our income and assets and the value of our assets from time to time (which may be determined, in large part, by reference to the market price of the ADSs, which has been and may continue to be volatile). Therefore, the risk of us being or becoming a PFIC will increase if during any taxable year our ADS price declines significantly.

Moreover, it is not entirely clear how the contractual arrangements for 2021 between our subsidiary, our variable interest entities and the shareholders of our variable interest entities should be treated for purposes of the PFIC rules, and we may have been a PFIC if our variable interest entities were not treated as owned by us for these purposes. In addition, the extent to which our goodwill should be characterized as an active asset is not entirely clear. We also hold a substantial amount of cash. Accordingly, there can be no assurance that we will not be a PFIC for our 2022 or any future taxable year. If we were a PFIC for any taxable year during which a U.S. taxpayer holds ADSs or ordinary shares, the U.S. taxpayer generally would be subject to adverse U.S. federal income tax consequences, including increased tax liability on disposition gains and "excess distributions," and additional reporting requirements. See "Item 10. Additional Information—10.E. Taxation—Material U.S. Federal Income Tax Considerations—Passive Foreign Investment Company Rules."

Item 4. Information on the Company

A. History and Development of the Company

In 2010, our founders launched 1 Drugstore, one of the first online retail pharmacies in China. In January 2013, Yihao Pharmaceutical Chain established its subsidiary Shanghai Yaowang E-Commerce Co., Ltd., or Shanghai Yaowang. In May 2013, Yao Wang Holdings Ltd. was incorporated under the laws of the Cayman Islands as our offshore holding company, which changed its name to New Peak Group in June 2015, and subsequently changed its name to 111, Inc. in April 2018. In June 2013, Yao Wang Corporation Limited, or Yao Wang, was incorporated in Hong Kong as a wholly owned subsidiary of 111, Inc. 1 Pharmacy Technology (Shanghai) Co., Ltd. (previously known as Yao Fang Information Technology (Shanghai) Co., Ltd. and 1 Pharmacy Yao Fang Technology (Shanghai) Co., Ltd.), or 1 Pharmacy Technology, was established in August 2013 as a wholly owned subsidiary of Yao Wang in the PRC. In September 2013, 1 Pharmacy Technology entered into a series of contractual agreements with Guangdong Yihao Pharmacy Co., Ltd., or Yihao Pharmacy, Yihao Pharmaceutical Chain and Shanghai Yaowang and their respective shareholders such that Yihao Pharmacy, Yihao Pharmaceutical Chain and Shanghai Yaowang were each treated as a variable interest entity of 1 Pharmacy Technology, and 1 Pharmacy Technology consolidated the financial results of Yihao Pharmacy, Yihao Pharmaceutical Chain and Shanghai Yaowang in its consolidated financial statements in accordance with U.S. GAAP.

Through 1 Pharmacy Technology, we obtained control over Yihao Pharmacy, Yihao Pharmaceutical Chain and Shanghai Yaowang, or collectively, the previous variable interest entities, based on a series of contractual arrangements. In February 2022, we obtained direct equity ownership in all of our previous variable interest entities through terminating such contractual arrangements, the details of which are described in the paragraphs below.

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In May 2018, Chongqing Yihao Pharmacy Co., Ltd. was established as a wholly owned subsidiary of Yihao Pharmacy in the PRC. In December 2018, Yihao Pharmacy transferred 100% equity interests in Chongqing Yihao Pharmacy Co., Ltd. to 1 Pharmacy Technology. In June 2018, Tianjin Yihao Pharmacy Co., Ltd. was established as a wholly owned subsidiary of Yihao Pharmacy in the PRC. In July 2018 and August 2019, Kunshan Yifang Pharmacy Co., Ltd. and Fujian Yaofang Pharmacy Co., Ltd. were also established as a wholly owned subsidiary of Yihao Pharmacy and Chongqing Yihao Pharmacy Co., Ltd. in the PRC, respectively. In August 2019, Chongqing Yihao Pharmacy Co., Ltd. purchased 100% of the equity interests in Hubei Yihao Pharmacy Co., Ltd. In March 2020, Chengdu Yizhen Internet Hospital Co., Ltd. was established as a wholly owned subsidiary of Kunshan Yihua Hospital Co., Ltd., a wholly owned subsidiary of Yihao Pharmaceutical Chain. In October 2020 and November 2020, Shanxi Yihao Yaofang Pharmacy Co., Ltd. and Liaoning Yihao Pharmacy Co., Ltd. were established as wholly owned subsidiaries of Chongqing Yihao Pharmacy Co., Ltd. in the PRC.

On September 15, 2018, our ADSs commenced trading on Nasdaq under the symbol “YI.” We raised from our initial public offering approximately US\$ 101.2 million in net proceeds (including the net proceeds generated from the offering of additional 809,555 ADSs upon the underwriters’ partial exercise of their over-allotment option), after deducting underwriting commissions and the offering expenses payable by us.

On August 17, 2020, 1 Pharmacy Technology completed the capital injection from new investors with an aggregate of RMB419.82 million (approximately US\$60.49 million). On December 22, 2020, 1 Pharmacy Technology completed another round of financing with an aggregate of RMB515 million (approximately US\$78.75 million). In connection with each round of the capital injection, the investors agreed to take all necessary and reasonable steps to facilitate the proposed listing of 1 Pharmacy Technology on the STAR Market. In the event that 1 Pharmacy Technology’s proposed listing on the STAR Market is not completed before June 30, 2023 or the date otherwise agreed by 1 Pharmacy Technology and the investors in writing, such investors may choose to exercise their options to require the controlling shareholder of 1 Pharmacy Technology, Yao Wang, to redeem all or part of the equity interests then owned by such investors.

In May 2021, Yijianyikang Medical Technology (Shanghai) Co., Ltd. (“Yijianyikang”), a wholly owned subsidiary of 1 Pharmacy Technology, initiated the 1 Health Membership program to reward and nurture relationships with the pharmacies that purchase products from us. Since May 2021, Yijianyikang and 1 Pharmacy Technology have entered into cooperation agreements with pharmacies that enrolled in the program and those pharmacies’ shareholders. Pursuant to each of such cooperation agreement, Yijianyikang granted to the shareholders of the relevant pharmacy options to purchase a certain number of shares in Yijianyikang that will vest over a four-year vesting period, subject to certain predetermined annual purchase target. Under certain circumstances, the shares in Yijianyikang that can be acquired through the vesting of the options will be converted into the shares of 111, Inc. at a specified conversion rate.

We historically operated our business through contractual arrangements with variable interest entities, or VIEs, based in the PRC, namely Yihao Pharmacy, Yihao Pharmaceutical Chain and Shanghai Yaowang in which we did not directly own any equity interests. During the term of such contractual arrangements, we were able to consolidate the financial results of the VIEs in our consolidated financial statements in accordance with U.S. GAAP. In 2019, 2020 and 2021, the amount of revenues generated by the VIEs accounted for 83.6%, 55.1% and 40.6%, respectively, of our total net revenues. As of December 31, 2020 and 2021, the total assets of the variable interest entities, excluding amounts due from other companies in the Group, equaled to 29.4% and 31.8% of our consolidated total assets, respectively. In February 2022, we terminated the contractual arrangements between 1 Pharmacy Technology and the VIEs, and Mr. Yue Xuan and Ms. Jing Liu, who were the shareholders of Yihao Pharmacy, transferred their equity interests in Yihao Pharmacy to 1 Pharmacy Technology. Following such termination and share transfer, all of the VIEs became our subsidiaries in which we had direct equity ownership.

Our principal executive offices are located at 3-5/F, No.295 ZuChongZhi Road, Pudong New Area, Shanghai, the People’s Republic of China. Our telephone number at this address is +86 21 2053 6666. Our registered office in the Cayman Islands is located at the offices of Vistra (Cayman) Limited, P.O. Box 31119, Grand Pavilion Hibiscus Way, 802 West Bay Road, Grand Cayman, KY1-1205, Cayman Islands. Our agent for service of process in the United States is Puglisi & Associates, located at 850 Library Avenue, Suite 204, Newark, Delaware 19711.

Recent Regulatory Development

Cybersecurity Review Measures

The PRC Data Security Law took effect on September 1, 2021, and numerous regulations, guidelines and other measures have been or are expected to be adopted under the umbrella of, or in addition to, the Cyber Security Law and Data Security Law. On December 28, 2021, the CAC and several other regulatory authorities in China jointly promulgated the Cybersecurity Review Measures, which came into effect on February 15, 2022. Pursuant to the Cybersecurity Review Measures, (i) if the relevant activity affects or may affect national security, a CIIO that purchases network products and services, or an internet platform operator that conducts data process activities, shall be subject to the cybersecurity review, (ii) an application for cybersecurity review shall be made by an issuer who is an internet platform operator holding personal information of more than one million users before such issuer applies to list its securities on a foreign stock exchange, and (iii) relevant governmental authorities in the PRC may initiate cybersecurity review if they determine an operator's network products or services or data processing activities affect or may affect national security.

As of the date of this annual report, uncertainties still exist in relation to the interpretation and implementation of the Cybersecurity Review Measures. Although we have not been identified as a CIIO by any regulatory authority, we cannot rule out the possibility that we, or certain of our customers or suppliers, may be deemed as a CIIO. If we are deemed as a CIIO, our purchases of network products or services, if deemed to be affecting or may affect national security, will need to be subject to cybersecurity review, before we can enter into agreements with relevant customers or suppliers, and before the conclusion of such procedures, these customers will not be allowed to use our products or services, and we are not allowed to purchase products or services from our suppliers. For details of the associated risks, see "Item 3. Key Information—3.D. Risk Factors—Risks Related to Our Business and Industry—Our business generates and processes a large amount of data, and complying with evolving laws and regulations regarding cybersecurity, information security, privacy and data protection and other related laws and requirements may be expensive and may force us to make adverse changes to our business. Many of these laws and regulations are subject to changes and uncertain interpretations, and any failure to comply with these laws and regulations could result in negative publicity, legal proceedings, suspension or disruption of operations, increased cost of operations, or otherwise harm our business."

As of the date of this annual report, we have not been involved in any investigations or become subject to a cybersecurity review initiated by the CAC based on the Cybersecurity Review Measures, and we have not received any inquiry, notice, warning, sanctions in such respect or any regulatory objections to our listing status from the CAC.

Privacy and Data Protection

The Personal Information Protection Law took effect on November 1, 2021, integrates the various rules with respect to personal information rights and privacy protection. Since September 2021, a series of laws and regulations relating to information security, privacy and data protection has been published. For more information about these laws and regulations, see "Item 4. Information on the Company—B. Business Overview—Regulations—Regulations relating to Internet Information Security and Privacy Protection." For details of the associated risks, see "Item 3. Key Information—3.D. Risk Factors—Risks Related to Our Business and Industry—Our business generates and processes a large amount of data, and complying with evolving laws and regulations regarding cybersecurity, information security, privacy and data protection and other related laws and requirements may be expensive and may force us to make adverse changes to our business. Many of these laws and regulations are subject to changes and uncertain interpretations, and any failure to comply with these laws and regulations could result in negative publicity, legal proceedings, suspension or disruption of operations, increased cost of operations, or otherwise harm our business."

Potential CSRC Approval and Filing Required for the Listing of Our ADSs

On July 6, 2021, certain PRC regulatory authorities issued Opinions on Strictly Cracking Down on Illegal Securities Activities. These opinions call for strengthened regulation over illegal securities activities and supervision on overseas listings by China-based companies and propose to take effective measures, such as promoting the development of relevant regulatory systems to deal with the risks and incidents faced by China-based overseas-listed companies. As of the date of this annual report, no official guidance and related implementation rules have been issued in relation to these recently issued opinions and the interpretation and implementation of these opinions remain unclear at this stage.

On December 24, 2021, the CSRC published the draft Administrative Provisions of the State Council on the Overseas Issuance and Listing of Securities by Domestic Companies (Draft for Comments), or the Administrative Provisions, and the draft Measures for the Overseas Issuance and Listing of Securities Record-filings by Domestic Companies (Draft for Comments) for public comments. These draft regulations stipulate that PRC domestic companies that seek to offer and list securities in overseas markets directly or indirectly shall complete the filing procedures with and report relevant information to the CSRC. Pursuant to these drafts, if the issuer meets the following conditions, its offering and listing will be deemed as an “indirect overseas offering and listing by a PRC domestic company” and is therefore subject to the filing requirement: (i) the revenues, profits, total assets or net assets of the Chinese operating entities in the most recent financial year accounts for more than 50% of the corresponding data in the issuer’s audited consolidated financial statements for the same period; (ii) the majority of senior management in charge of business operation are Chinese citizens or have domicile in PRC, and its principal place of business is located in PRC or main business activities are conducted in PRC. The domestic enterprises should submit filing documents to CSRC within three business days after the submission of the application for overseas initial public offering, and after completing the filing procedures for an overseas initial public offering and listing, for the purposes of implementing and strengthening the CSRC’s supervision, the issuer will need to comply with continuous filing and reporting requirements after such offering and listing, among others, including the following: (i) reporting material events which arose prior to such offering and listing, (ii) filing for follow-on offerings after the initial offering and listing, (iii) filing for transactions in which the issuer issues securities for acquiring assets, and (iv) reporting material events after the initial offering and listing. However, the Draft Overseas Listing Regulations and the Draft Overseas Listing Measures were released for public comment only, there remains substantial uncertainty, including but not limited to its final content, adoption timeline, effective date or relevant implementation rules. As of the date of this annual report, we cannot predict the impact of these regulations on maintain the listing status of our ADSs and/or other securities, or any of our future offerings of securities overseas in a foreign country.

We cannot assure you that we will not be required to obtain the approval of or complete the filing with the CSRC or other regulatory authorities to maintain the listing status of our ADSs on the Nasdaq or to conduct overseas securities offerings in the future. For details of the associated risks, see “Item 3. Key Information—3.D. Risk Factors—Risks Related to Doing Business in China—The approval, filing or other requirements of the China Securities Regulatory Commission or other PRC government authorities may be required under PRC law in connection with our issuance of securities overseas.” We have been closely monitoring regulatory developments in China regarding any necessary approvals from the CSRC, the CAC, or other PRC regulatory authorities required for overseas listings and securities offerings. As of the date of this annual report, we have not received any inquiry, notice, warning, sanctions or regulatory objection from the CSRC in this regard.

B. Business Overview

In 2010, our founders launched 1 Medicine Marketplace (1 药网), one of the first online retail pharmacies in China. Today, we provide hundreds of millions of consumers with better access to pharmaceutical products and medical services, directly through our online retail pharmacy and indirectly through our offline pharmacy network. In 2016, we commenced our online medical services through our internet hospital, 1 Clinic (1 诊), to provide consumers with cost-effective and convenient online consultation and electronic prescription services. Our online wholesale pharmacy, 1 Pharmacy (1 药城), serves as a one-stop shop for pharmacies, clinics and hospitals, among others, to source a vast selection of pharmaceutical products.

Our New Retail Platform

New Retail aims to improve the efficiency of selling and buying, as well as customer experience, by integrating e-commerce, brick-and-mortar retail, and logistics with data throughout the value chain. In 2016, we began the transformation from a pure B2C business to a New Retail platform, integrating our online retail pharmacy and offline pharmacy network by leveraging our smart supply chain and cloud-based solutions. This model allows us to collect and analyze data from a large number of transactions, which we use to continuously increase the efficiency of our smart supply chain, and the intelligence of our cloud-based solutions.

Our Ecosystem

We connect pharmacies, pharmaceutical companies, medical professionals, insurance companies and consumers in our ecosystem, and we improve the efficiency and transparency of the pharmaceutical value chain. We create value for various participants in our integrated online and offline platform in the healthcare ecosystem in China: (i) consumers who purchase pharmaceutical and other health and wellness products and seek medical services; (ii) pharmacies, including independent pharmacies, pharmacy chains and in-house pharmacies within clinics and private hospitals who purchase pharmaceutical products and interact with consumers through our platform; (iii) suppliers, such as pharmaceutical companies and distributors; (iv) marketplace sellers, who use our platform to distribute and sell their products; (v) insurance companies, which are integral to the roll out of our new closed-loop internet “healthcare + pharma” pharmacy benefits management model and (vi) medical professionals who provide healthcare services through our platform.

Our Omni-channel Model

Our omni-channel model plays an important role in facilitating the commercialization of drugs across the nation. Partners in this model include pharmacies, public and private hospitals, clinics, community health centers, distributors, medical representatives and our 1 Medicine Marketplace app. This model offers multiple channels for pharmaceutical companies to simultaneously reach healthcare providers nationwide and educates them about new drugs and therapies. This model significantly reduces time, resources and cost, which allow drugs to be distributed quickly and efficiently.

Our S2B2C Model

Our S2B2C model refers to “Supply Chain Platform” to enable “Business” to better serve “Customers”. We developed this business model with unique advantages, unrivalled national sales network and coverage, fast growing partnerships with world class supply chain, and an ecosystem powered by its state-of-the-art digital platform to capitalize on this massive market.

We developed the supply chain infrastructure, the “S” that enables the model. Since our inception, we have built an innovative digital platform that would allow us to benefit from disrupting the status quo. Our supply chain infrastructure also encompasses the network of suppliers, pharmaceutical companies, distributors, marketplace vendors and other service providers.

This infrastructure is digitally connected to our rapidly growing network of retail pharmacies, one of the “B”s in our model, offering them the capability for vast selection of products and assortment, SaaS tools, CRM, cloud clinic, speedy home delivery services, all of which enable them to better serve customers with enhanced efficiency and the reduced cost. The same supply chain platform is also designed to bring value to doctors, the other “B” in our model. They are able to enjoy our service modules of cloud clinic, cloud pharmacy, doctor-patient platform to provide follow-up care to patients, which improves the doctor-patient experience and drives positive care outcomes. On our platform, geography will no longer be a limitation, preventing doctors from engaging and interacting with their patients. Conducting regular post-discharge consultation and online refill of medicine can help reduce readmissions by detecting and mitigating potential complications early.

Having established a robust foundation, we extended this model to bring value to patients, the “C” in S2B2C, by digitally connecting them to medicines and the healthcare services. Through our supply chain platform, doctors and pharmacies are able to leverage different service modules to offer a variety of services to patients.

We take great pride in creating a platform where customers from all around the country can enjoy either pure digital or a combination of online plus offline services, which leads to better health outcomes.

Our Products and Services to Consumers

Our Online Retail Pharmacy

Our online retail pharmacy is an integral part of our holistic online and offline platform. In 2010, our founders launched our online retail pharmacy, 1 Medicine Marketplace, to fulfill the healthcare needs of consumers. 1 Medicine Marketplace is currently available through our 1 Medicine Marketplace app or website. We provide consumers with a wide variety of pharmaceutical products and other merchandise, including drugs, nutritional supplements, contact lenses, medical supplies and devices, personal care products as well as baby products. We operate our online retail pharmacy under either direct sales model or the marketplace model.

Our Direct Sales Model

In our online direct sales model, we acquire products from suppliers and sell them directly to consumers. For this model, we need to manage inventories to ensure effective inventory management and may adjust inventory level based on fluctuation in supply and prices, seasonality, popularity of a particular product, and we also take into consideration the shelf life. See “—Supply Chain Management—Inventory Management.” Under this model, we also operate our independent branded storefronts in leading e-commerce platforms in China such as Tmall.com, JD.com and PDD.com. We pay these third-party e-commerce platforms commissions as a percentage of sales.

Our Marketplace Model

We introduced an online marketplace in 2016 to leverage our brand recognition, large and growing customer base, and proprietary technology platform. Under our marketplace model, third-party sellers offer products to consumers over our online marketplace.

We facilitate transactions between marketplace sellers and consumers through our marketplace. We provide transaction processing and billing services on all orders on our online marketplace, while the marketplace sellers are responsible for inventory management, fulfillment and delivery. We require marketplace sellers to meet our standards for authenticity and reliability. We aim to offer consumers the same high quality customer experience regardless of the source of the products they choose.

We collect commission fees and platform usage fees from marketplace sellers according to the terms of our individual contracts with them. The commission fees are generally charged as a percentage of sales, depending on product category, among other things. We also charge a fixed annual platform usage fees to marketplace sellers for maintaining storefronts on our platform. We provide order processing services for all orders on our online marketplace.

Our Offline Retail Pharmacy

We also operate a network of offline retail pharmacies branded as “Yi Hao Pharmacy,” mainly in Guangdong province, which enables us, as required by the relevant laws and regulations, to operate our online pharmaceutical retail businesses. As of December 31, 2021, we had 14 offline retail pharmacies in Guangzhou, Tianjin, Kunshan, Chongqing and Wuhan. Revenue contribution from our Yi Hao Pharmacies was insignificant in 2019, 2020 and 2021.

Our Drug Benefit Plan

We provide our drug benefit plan for our chronic patients. Under this plan, our online doctors and pharmacists maintain regular contact with members to provide them with systemized online consultation, on-line prescription refill, medication guidance, information on symptoms, outreach for feedback, and real-time drug and nutrition recommendation. Members may also purchase brand-name drugs at a discount. This plan significantly improves medication adherence rates and repurchase rate.

Our Product Offerings to Consumers

We carry diverse and comprehensive products in our online retail and offline retail pharmacies. Our unique integrated retail and wholesale supply chain and inventory management combines the management of retail and wholesale SKUs. The merchandise offered by us and the marketplace sellers can be broadly classified into the following major categories:

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Drugs. We display drugs, including prescription drugs and over-the counter, or OTC, drugs such as western medicines and traditional Chinese medicines.

Nutritional supplements. We display nutritional supplements, including a variety of vitamins, and dietary products.

Contact lenses. We offer a comprehensive selection of contact lenses that cover all major brands.

Medical supplies and devices. We offer a variety of general-purpose medical supplies and devices such as bandages and thermometers.

Other products. Our other products include personal care products such as skin care, birth control, sexual wellness products as well as baby products.

We also sell seasonal and promotional items tailored to local consumer demand for convenience and quality. In 2017, we further expanded our product offerings by introducing more health and wellness products and smart wearable devices. We believe that offering these products increases the order size spend per visit by meeting the growing demand for one-stop shopping convenience.

Consumers can browse our products by category or scan barcodes of drugs they find in store and easily find them on our online retail pharmacy.

Pricing and Payment of Products

We offer competitive pricing to attract and retain consumers. Under the direct sales model, prices are set by us with reference to major online and offline competitors, taking into account our overall pricing strategy for different categories. We believe our prices are generally lower than those of offline pharmacy chains and independent pharmacies. We constantly monitor the prices of products offered by our competitors through our pricing intelligence system. See “—Technology and IT Infrastructure— Cloud-based Applications.” Under our marketplace model, sellers are free to set their own prices, but are encouraged to set comparable and competitive prices. We also occasionally offer significant discounts on certain products for a limited time in flash sales or other promotional activities, including our anniversary sale and “November 11 sale.” We make continuous efforts to maintain and improve an efficient cost structure and create incentives for our suppliers to provide us with competitive prices.

We provide our consumers flexible payment options for both direct sales and marketplace models. Our payment options include in-person settlement (which is required and the only option for the purchase of prescription drugs), bank transfers, online payments with credit cards and debit cards, and payment through third-party online payment platforms, such as WeChat Payment and Alipay. For fulfillment and delivery options, please see “—Supply Chain Management—Fulfillment and Delivery.”

Our Online Consultation and E-prescription Services

We strive to provide our consumers with convenient access not only to pharmaceutical products, but also to medical services. We commenced our online consultation services, through 1 Clinic, a licensed internet hospital operated by us, in 2016, to address the need for cost-effective and convenient evaluation of health and medical conditions. Our online consultation utilizes a user-friendly interface embedded in 1 Medicine Marketplace website and app designed to empower consumers to remotely access healthcare. This service covers a wide range of conditions and cases, with a primary focus on common and chronic illnesses. For conditions that require in person or further examination or laboratory testing, we generally refer our consumers to hospitals.

Consumers access our online consultations primarily through photo and text consultations, phone calls and video consultations. They can select a doctor of their choosing based on the doctor’s availability and his/her profile displayed on our platform. Our photo and text consultation sessions are offered to consumers for free. We typically charge a fixed amount of fees per consultation session for consultations through video and online assisted telephone calls, which differ based on the type of consultation used and are paid through our convenient online payment system.

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The first step to utilize our services is to provide basic personal information, descriptions of conditions and any medical records or laboratory test results through our online platform. Based on the consumer's response to inquiries on the condition at issue, the doctor provides medical recommendations, issues prescriptions, or advises the consumer to have an examination conducted at a hospital and uploads the results to our system.

We provide ongoing training and professional development programs to our in-house medical professionals. We conduct weekly evaluations of our in-house doctors and medical assistants in respect of quality of service, user feedback and efficiency. We have also adopted a quality control system with standardized protocols for our services performed by our in-house medical team. We contract services from external doctors who practice at reputable hospitals with significant experience and appropriate credentials. We require external doctors to register with us and to agree to our terms of use, pursuant to which they must comply with both our specified work scope and quality requirements, and the applicable rules and regulations. See “—Risk Management and Internal Control—Healthcare Service Quality and Safety.”

We offer e-prescription services to consumers as an integral part of the online consultation process, subject to our stringent compliance procedures. Each of our prescriptions is issued by qualified doctors. The e-prescription services is also available when a consumer needs to purchase a prescription drug through the offline pharmacy network. See “—Our Products and Services to Pharmacies—Our Cloud Prescription Services.”

Customer Service and Satisfaction

Providing satisfactory customer services is a high priority. Our commitment to consumers is reflected in the high service quality provided by our customer service staff and speedy fulfillment and delivery services. We have high levels of customer satisfaction, as evidenced by a customer satisfaction rate over 99% on 1 Medicine Marketplace in 2021.

Our Products and Services to Pharmacies

We have enabled more than 385,000 offline pharmacies, as of December 31, 2021, to better serve their consumers. The pharmacy customers we serve include small and medium-sized retail pharmacy chains, independent pharmacies and in-house pharmacies within clinics and private hospitals, spanning across 31 provinces in China.

Our Online Wholesale Pharmacy

We provide comprehensive, intelligent and integrated distribution solutions through our online wholesale pharmacy, 1 Pharmacy, available both through our 1 Pharmacy app and website. Overall, our business involves a process of sourcing from suppliers, warehousing, processing orders and invoicing, payment collection and delivering to pharmacies. These pharmacy customers include independent pharmacies, pharmacy chains, in-house pharmacies within clinics and private hospitals, as well as certain select distributors that have both retail and wholesale businesses.

1 Pharmacy features an extensive selection of pharmaceutical and other health and wellness products sourced from pharmaceutical companies and other suppliers. A substantial majority of prescription and OTC drugs displayed on 1 Pharmacy are available under our direct sales model. Our broad and fast-growing product offerings enable us to satisfy the purchasing needs of our pharmacy customers. Meanwhile, our strong sourcing capability, coupled with our highly cost-effective distribution model, enables us to bypass traditional layers of the distribution network to provide competitive prices to our pharmacy customers.

Our Direct Sales Model

We primarily conduct our wholesale distribution business through our direct sales model, where we procure pharmaceutical products from pharmaceutical companies or distributors and sell to our pharmacy customers. As of December 31, 2021, we directly sourced from 515 pharmaceutical companies . Leveraging our strong relationship with our suppliers, we offer a comprehensive selection of pharmaceutical products at market-competitive pricing. Under the direct sales model, we are responsible for the fulfillment and delivery of the products sold.

Our Marketplace Model

We also operate an online marketplace where third-party sellers can directly sell to pharmacies. These marketplace sellers primarily consist of traditional offline distributors. They leverage our platform and customer base to grow their business, while at the same time complementing our product offerings under our direct sales model. Our marketplace business model under our wholesale business is similar in many respects to our retail business, including the charging model. For a detailed discussion, please see “—Our Products and Services to Consumers—Our Marketplace Model.”

Our 1 Health Membership Program

We launched the 1 Health Membership program in May 2021 to reward and nurture relationships with the pharmacies that purchase products from us. Our 1 Health Membership program is a membership model that effectively connects pharmaceutical companies with pharmacies and patients to empower small-to-mid size pharmacy chains. As a crucial part of our S2B2C model, this program allows members who participate in this program to enjoy privileged benefits, including exclusive access to our vast selection and competitive prices, access to our proprietary systems that can help them manage inventory, optimize procurement process and improve product selection and assortment. The members are required to connect their ERP systems to our 1 Health Platform which is operated by Yijianyikang. We do not charge any membership fees. In order to incentivize these pharmacy chains to participate, the shareholders of the pharmacies that enrolled in the program were granted options to purchase a certain number of shares in Yijianyikang, one of our subsidiaries. For further details, see Item 4. Information on the Company-A. History and Development of the Company.” As of December 31, 2021, we had over 11,000 participating pharmacy stores.

Payment, Exchange and Return

We generally require advance payment or payment-upon-delivery for purchases. For certain select pharmacy customers, we may grant a credit period of up to a month. We generally do not offer product return and exchange service unless the damages are caused by our fault.

Supply Chain Finance Service

We offer convenient online loan application services to the clients of 1 Pharmacy, including pharmacies and wholesalers, when they purchase drugs on 1 Pharmacy. Our service provides access to credit loans from a third party at low interest rates, which can effectively alleviate the clients’ cash flow pressures, subsequently increasing their purchase frequency and order size.

Our Cloud-based Inventory Management Services

Most of our pharmacy customers, in particular, independent pharmacies and in-house pharmacies within clinics and private hospitals, do not have a comprehensive inventory and demand forecast system. Purchases by these customers are primarily made based on historical experience, and their inventory turnover days are generally long due to a lack of detailed, precise planning and bulk purchase patterns. In addition, their inventory level is subject to fluctuations as a result of seasonal or other factors beyond their control.

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Our online wholesale pharmacy, featuring a vast selection of pharmaceutical products and speedy delivery, enables cloud-based inventory management. Pharmacy customers, rather than relying on advance but often imprecise planning, can collaborate with us for inventory visibility and on-demand offering. We simplify and streamline the procurement process and shorten the procurement cycle. Our pharmacy customers typically do not need to negotiate or enter into any purchase and sale agreement or make any purchase commitment. The purchase orders of our pharmacy customers on 1 Pharmacy are processed in real time. Typically, the order processing will take within 15 minutes, after which orders will be dispatched for delivery through our fulfillment network. The inventory on demand and just-in-time delivery offer significant benefits to our pharmacy customers. Instead of bulk purchases and maintaining large inventory, pharmacies procure their inventory with more precision, reducing their working capital needs and enabling them to quickly respond to market demand. As a result, we are able to improve the inventory turnover of our pharmacy customers.

Our Cloud Pharmacy Services

We help offline pharmacies to build their online presence effectively and to extend the reach of their products to cover a broader consumer base through the Internet, thus expanding their market coverage and improving their service capabilities.

Our Cloud Clinic Services

We enable offline pharmacies to provide online consultation and e-prescription services through our cloud clinic services to patients.

Our Cloud Prescription Services

Pharmacies, especially independent pharmacies and small-to-medium sized pharmacy chains, often lack onsite doctors to offer prescriptions to consumers with minor ailments or chronic diseases visiting their stores. In 2018, we began to use our cloud prescription services to leverage our existing online consultation and e-prescription service platform to offer convenient online consultation services to these consumers onsite. Once consumers obtain their prescriptions from us, they will be able to purchase prescription drugs from our pharmacy customers. In return for our services, we charge our pharmacy customers a fixed amount of annual service fees. The annual service fees vary, depending on the number of online consultations performed, the number of e-prescriptions issued, and the number of drugs purchased in connection with our services.

Our Smart Procurement Services

Leveraging our extensive experience in inventory management and our data analytics capabilities, we launched our smart procurement services in the first quarter of 2018 to cooperate with pharmacies to collect their historical purchase orders and inventory data. We then typically analyze historical purchase patterns, the location of the pharmacy and regional supply and demand information, any epidemic status and trend, and current pricing and promotions. Through our proprietary big data analytic platform and sophisticated prediction model, we can make individualized purchase recommendations for our pharmacy customers' review.

Given our broad reach within the pharmaceutical value chain, we believe that we will be able to detect trends in the industry and forecast demand, therefore, meeting the procurement needs of pharmacies through our customized generated purchase orders. Our smart procurement service is also capable of comparing prices across different sellers on our platform to ensure the best pricing for our pharmacy customers. As pharmacy customers gradually increase the use of our services, we believe that we can accumulate data to optimize our own supply chain management, while providing better solutions to both pharmacies and upstream suppliers with more relevant service offerings.

Our Automated Salesforce Tool

Hawkeye is an automated tool that we provide to our on-the-ground sales team to better serve customers. This tool captures the behavior of every pharmacy customer that surfs the 111 website, and monitors the supply chain status on a real-time basis. For example, upon replenishment of an SKU, Hawkeye will immediately generate a task for our sales team to engage customers who have researched, or who have searched for this SKU in the past. This tool enables our sales team to identify the purchase intent of pharmacies more intuitively and to offer more customized recommendations. As a result, our on-the-ground sales coverage efficiency improved threefold.

Customer Experience

We are committed to optimizing and achieving satisfaction of our pharmacy customers. This commitment drives every aspect of our operations, which are focused on five core components: extensive product offerings, competitive pricing, transformational online procurement processes and frequent customer engagement, as well as timely and accurate fulfillment. We also build customer loyalty and encourage pharmacies to make repurchases by actively engaging with them. After assisting our pharmacy customers to open accounts and establishing initial relationships, our on-the-ground sales force frequently liaise with these pharmacies via in-person visits, telephone calls or other social network tools to share the latest promotional information and drive repeat purchases.

Our Services to Pharmaceutical Companies

We source products from pharmaceutical companies and distributors, while at the same time providing them with data services and other value-added services.

Data Services

Leveraging our direct reach to many touchpoints of the healthcare and pharmaceutical value chain, we launched our data services in 2018 on a pilot basis to help our pharmaceutical companies expand their reach and gain valuable insights to the distribution channel and consumers. We compile, aggregate and analyze our detailed sales data to uncover purchase patterns and predict future purchase behaviors and demand. With our broad consumer base, we can extract valuable information from our extensive database. For a particular product, we analyze the regional and seasonal sales patterns, the amounts of orders, the frequency of purchases, any particular preference for packaging, and other factors that may affect sales. Data mining of our available data is a powerful tool to predict consumer behaviors and market trends, allowing pharmaceutical companies to make knowledge-driven decisions in their sales forecasts and budgeting. For a discussion of our pricing intelligence system, see “—Technology and IT Infrastructure—Cloud-based Applications.”

Supply Chain Integration Services

Leveraging our established supply chain system, we provide supply chain integration services to help pharmaceutical companies manage their products through online and offline distribution channels. In addition to our supply chain integration service, we also provide product promotion services, customer analytic services, patient education services and brand awareness services.

Our Services to Medical Professionals

We provide medical professionals with services to enable them to better serve patients and improve service quality.

E-medical Record and Patient Management

We create and maintain, in secured electronic storage, a copy of electronic medical records for certain consumers. These e-medical records allow consumers to access past consultation history and communicate with doctors for follow-up or new consultations. Our cloud-based platform and e-medical record services also enable more efficient patient management by doctors. Doctors use our system for reviewing e-medical records with the patient’s consent.

Suppliers

We have an extensive network of suppliers, consisting primarily of pharmaceutical companies and distributors. As of December 31, 2021, we directly sourced from 515 pharmaceutical companies. We believe that competitive sources are readily available for substantially all of the merchandise we carry on our platform, and we have diversified our procurement sources to obtain more favorable terms and minimize our inventory risk.

Supplier Selection

When choosing suppliers, we take into consideration, among other things, whether their products complement our overall product offering, the quality and prices of their products, market reputation, production and/or distribution capacity and the market potential of their products. Before we engage with any new supplier, we also examine their qualifications and licenses to verify that they operate their businesses in compliance with applicable laws, rules and regulations.

Our Relationship with Pharmaceutical Companies and Key Suppliers

We have dedicated teams that work closely with our top suppliers, especially pharmaceutical companies, to strengthen our relationships with them. For the same product, the price from a pharmaceutical company is generally lower than from a distributor. We aim for qualification by major pharmaceutical companies as a “tier one” distributor so as to directly source from them. As of December 31, 2021, we have obtained such qualifications from 515 pharmaceutical companies and directly source from them. We also seek to cooperate with other “tier one” distributors who may have negotiated attractive prices for particular products. Our cooperation with these suppliers allows us to expand our product offerings and procure products manufactured by pharmaceutical companies without an established relationship with us. We intend to help pharmaceutical companies expand their end user base by leveraging our network of pharmacies. We also provide them with customized channel management services, as well as data flow, operational support, marketing, user data analysis and other value-added services. Together with pharmaceutical companies, we work to develop medical know-how including academic content and product trainings.

Supply Chain Management

We combine advanced technologies and supply chain optimization techniques to integrate the front and the back end of the supply chain and optimize our inventory management. Our unique integrated retail and wholesale supply chain and inventory management allow us to share inventories among 1 Medicine Marketplace, 1 Pharmacy, and Yi Hao Pharmacy, significantly increasing our operational efficiency. Supported by our proprietary supply chain management systems, efficiently designed supply chain protocols and processes, strategically located fulfillment centers and nationwide fulfillment network, our supply chain enables inventory on demand and just-in-time delivery for our consumers. As a result of our advanced supply chain management system, we have seen tangible improvements in our own and our customers’ efficiency levels.

Supply Chain Technologies and Systems

Our supply chain management system consists of four separate subsystems supported by proprietary software that allows us to effectively collaborate with third-party service providers and interact with our consumers and pharmacy customers. All of our systems are designed to comply with Good Supply Practices (GSP) for pharmaceutical products, and connect with provincial food and drug administrations for real-time monitoring.

Warehouse Management System (WMS). We customize our proprietary warehouse management system to meet the specific needs of our pharmaceutical distribution business. Our WMS enables us to closely monitor each step of the fulfillment process from guiding inventory receiving and put-away, optimizing picking and shipping of orders and advising on inventory replenishment. Our advanced WMS software optimizes our warehouse space and employees’ time, supports paperless material handling in a digital WMS environment and automates the interaction between our employees and material handling equipment, such as conveyor belts. For example, we developed advanced algorithms to optimize picking, packing and shipping. At each fulfillment center, inventory is bar-coded and tracked through our management information system, allowing real-time monitoring of inventory levels across our fulfillment network and item tracking at each fulfillment center. Our shelf space hosts the same inventory for both our wholesale and retail businesses, while the assignment and allocation logics are designed to cater to the different requirements for fast-moving and long-tail products, optimizing fulfillment efficiency. The seamless connection with our other supply chain management modules has led to increased inventory accuracy, greater space utilization, increased warehouse productivity and improved customer service.

Transportation Management System (TMS). Our transportation management system enables full operational control and visibility from dispatch to delivery, and from invoicing to receivables collections. Our TMS is integrated with third-party accounting systems. All of these systems are customer-oriented and allow for full shipment tracking and visibility, as well as for customer shipment input.

Procurement Management System (PMS). Our procurement management system promotes transparency and compliance. It consists of various modules with different levels of authorizations to different personnel. We are in the process of developing our data

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platform that is fully compatible with and can connect to many of our suppliers' ordering systems to allow seamless information exchange. We expect the new system to enhance the efficiency of various aspects of our purchase process, such as stocking and account settlement.

Order Management System (OMS). Our order management system allows us to manage inventory cost and pricing, and process orders from both pharmacy customers and consumers. It also provides us with flexible pricing and promotions to satisfy our customers' needs. Our order management system enhances our visibility into our customers' preferences, merchandise and supply chain, resulting in improved customer service, improved operational efficiency, enhanced management analytics and increased inventory synergies.

Price Intelligence System (PIS). Our price intelligence system generates price indexes and optimal pricing recommendations for products on 1 Pharmacy and 1 Medicine Marketplace by analyzing product information collected from online and offline channels, and makes automatic adjustments to prices based on optimal pricing strategies. Our PIS also provides clients with pricing data intelligence generated from our collection and analysis of products and prices on the market, useful in our clients' product procurement and pricing processes.

Inventory Management

We manage our inventory, both retail and wholesale, in an integrated manner. Our inventory, fulfillment and delivery services are centrally managed from our headquarters. Our inventory management allows our retail and wholesale businesses to access and share all of our inventory resources.

We continually seek to improve our inventory control and minimize inventory risk. We analyze historical sales data and days in inventory to establish inventory management plans. We may adjust our inventory management plans based on factors such as fluctuations in supply and prices, seasonality and sales of a particular product. Our inventory optimization model uses sophisticated algorithms to help determine when to replenish an SKU. We also perform regular spot inventory counts in our fulfillment centers. We monitor the shelf life of our pharmaceutical products by conducting periodic reviews, and either make sales promotion plans or make inventory write-downs depending on the status of the inventory.

Our inventory includes high level of stock for certain products that we consider as strategic reserves. These products are generally purchased at favorable price terms, and have a long shelf life. They also help us preempt possible industry-wide shortages.

Fulfillment and Delivery

As of December 31, 2021, our fulfillment network consists of eight regional fulfillment centers strategically located in Guangzhou in Guangdong Province in Southern China, Kunshan in Jiangsu Province in Eastern China (which is within close proximity of Shanghai), Tianjin in Northern China, Chongqing in Western China, Wuhan in Central China, Fuzhou in Fujian Province in Southern China, Xi'an in northwest China and Shenyang in northeast China. In the future, we plan to further improve the automation level and operation efficiency of these fulfillment centers.

We leverage our large-scale operations and reputation to obtain favorable contractual terms from third-party delivery companies. To reduce the risk of reliance on any single delivery company, we typically contract with two or more regional delivery companies in each major city. We regularly monitor and review the delivery companies' performance and their compliance with our contractual terms. In addition, we typically require the delivery companies to pay deposits or provide payment guarantees before providing services to us. We typically negotiate and enter into logistics agreements on an annual basis.

We are generally able to deliver to major cities in 31 provinces within 24 hours, and nationwide within 72 hours.

Risk Management and Internal Control

We have adopted and implemented various policies and procedures to ensure rigorous risk management and internal control, and we are dedicated to continually improving these policies and procedures.

Our risk management and internal control policies and procedures cover various aspects of our business operations such as product safety, healthcare quality and safety, regulatory risk management, government affairs and regulatory compliance.

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Product Quality and Safety

We place strong emphasis on quality and safety of the products we sell on our platform. We conduct random quality inspections of products we procure, and reject the shipment if it fails to meet our quality standards. Our quality control department rigorously implements quality control procedures.

Healthcare Service Quality and Safety

We value the quality and safety of the healthcare services we provide. We strive to minimize medical risks arising from our operations. We have never received any written notice or penalty for material non-compliance or violation of healthcare service quality and safety laws or regulations, nor have we received any recommendation for improvement with respect to healthcare service quality and safety from any government authority.

The skills, competence and attitude of our in-house medical team are essential for the quality of care that our users receive. We continually monitor the risk in relation to services provided by our in-house medical team to ensure the risk management policies and procedures have been strictly followed, so as to achieve effective and efficient governance, risk and control processes.

We have adopted stringent hiring procedures for doctors, pharmacists and medical assistants, which involve in-person interviews and assessments of technical knowledge. Our in-house medical team receives regular training on relevant safety policies, standards, protocols and procedures and is required to strictly comply with them in all aspects of our operations. We conduct frequent evaluations of our in-house doctors, pharmacists and medical assistants.

For external doctors, we generally require them to provide us with their qualifications and licenses and to strictly adhere to the work scope and quality requirements specified in their service agreements in compliance with applicable legal and regulatory requirements.

For healthcare institutions to which we refer our consumers, we consider a variety of factors such as reputation, scale of business, service quality and capability, as well as their facilities. We typically require healthcare institutions who cooperate with us to maintain requisite licenses, comply with relevant laws and regulations and follow our service guidelines. We also carefully monitor feedback from our consumers on the services provided by these healthcare institutions, and take that into consideration when determining our continued cooperation with such healthcare institutions. We are not responsible for any losses to our consumers resulting from disputes or breach of obligations in relation to the provision of the relevant services.

Regulatory Compliance and Risk Management

We have a dedicated public relations department, consisting of government relations and public relations teams and with a leader who has over 10 years of experience in regulatory compliance and risk management in Fortune 500 companies. We have designed and adopted strict internal procedures to ensure compliance of our business operations with all relevant laws and regulations and have established a code of conduct to regulate employee behavior and activities. In addition, we continually review the implementation of our risk management policies and measures to ensure our policies and implementation are effective and sufficient.

We work closely with relevant government agencies that have jurisdiction over our business. We maintain frequent communications with government agencies before implementing new business initiatives or when regulatory uncertainties arise as new laws or regulations are promulgated. We actively provide our inputs on proposed regulations that are subject to public comments. We are often invited to comment on proposed regulations by relevant government authorities during the comment solicitation process.

As part of our risk management and internal control measures, we have adopted a series of internal regulations against corrupt and fraudulent activities, which include measures against receiving bribes and kickbacks, and misuse of company assets. We have anti-corruption and anti-bribery clauses in a majority of our major business contracts, and we require our suppliers and other third parties who cooperate with us to comply with relevant laws and regulations.

Data Privacy and Protection

We are committed to protecting information and privacy of our consumers and other participants on our platform. We have developed a company-wide policy on data security to preserve individual personal information and privacy. We strictly comply with

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laws and regulations and do not distribute or sell our users' personal data for any purpose. We encrypt user data in network transmissions and in backend storage to ensure confidentiality. To minimize the risk of data loss, we conduct regular data backup and data recovery tests. Our database can only be accessed by certain designated and authorized personnel after assessment and approval procedures, whose actions are recorded and monitored.

Technology and IT Infrastructure

Our proprietary technology is one of our core competitive advantages. As of December 31, 2021, our technology and IT team consisted of 295 employees, including core team members with extensive experience with leading internet, online retail and e-commerce companies in China. We have built our technology platform primarily relying on proprietary software and systems that we have developed in-house. We develop and maintain various online platforms that connect the respective systems of various participants in the healthcare ecosystem, enabling them to access our services and connect with other participants in the ecosystem. As a result, they are able to conveniently share information and conduct their operations efficiently over our platform.

Data Collection, Aggregation and Analytics and Transaction Support

Our data assets are the backbone of our data analytics capabilities. We collect data under various scenarios across the entire pharmaceutical value chain. The high volumes of traffic over our platform have brought us large amounts of data, collected with the consumer's due authorization. Our strong data mining and user behavior analytics capabilities allow us to build a comprehensive profile for each consumer. Data analytics is extensively used in various aspects of our operations.

In addition, we collect a wealth of data on our supply chain, such as cost per delivery, delivery time requirements, positive customer feedback and other similar indicators. Based on our extensive database of supply chain information, we create operational goals and insights, including optimal time by which deliveries must be made to elicit positive consumer feedback and optimal delivery routes that minimize cost per delivery. We use the data we possess to simplify supply chain management, enabling our business to operate more efficiently, giving us more visibility and control over our inventory and reducing our operational costs. For discussion of our supply chain management and related technologies, please see "—Supply Chain Management."

Cloud-based Applications

Our platform is built on highly scalable and reliable cloud-based technology architecture that can accommodate the increasing scale and complexity of our business operations. Our IT framework includes service-oriented architecture, business intelligence, single sign-on, ERP Open API, pay component, image recognition, message-oriented middleware, task scheduling center and radio frequency identification, or RFID. Service-oriented architecture is a style of software design where services are provided to the other components by application components. ERP Open API is standardized API, or application programming interface, that is compatible with different ERP systems adopted by pharmacy customers. Message-oriented middleware is a software or hardware infrastructure that supports sending and receiving messages between distributed systems, allowing application modules to be distributed over heterogeneous platforms and reducing the complexity of developing applications that span across multiple operating systems and network protocols. We are able to rapidly enroll consumers, pharmacy customers and suppliers onto our platform and seamlessly include them in our system.

Our sophisticated CRM system enables us to effectively gather, analyze and use customer data to plan customized marketing activities. In addition, we also provide our data insights to pharmacies and marketplace sellers to help them optimize their sales and marketing strategies. Our CRM system enables us to reduce costs and increase profitability through increased customer loyalty and attention. Our online platform for doctors also has a CRM system and lays the foundation of patient management and assists the interaction between medical professionals.

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Our business intelligence system provides operational analysis, sales forecasts and other application-oriented intelligent products that facilitate data-driven decision making. One such application is our pricing intelligence system, which applies data mining techniques to discover, match, extract and report on competitive pricing data to optimize our pricing strategy relative to our competition. This pricing intelligence system helps us gain a better understanding of our price position in the market and make automatic adjustments to thousands of our SKUs. We also use our pricing intelligence system to provide data services to pharmaceutical companies. See “—Our Services to Pharmaceutical Companies.”

Our IT Infrastructure

We are committed to maintaining a secure online platform. We have built a firewall that monitors and controls incoming and outgoing traffic on our platform 24/7. Once any abnormal activity is detected, our system will immediately notify our IT team and simultaneously take automatic protective and remedial measures, such as activating third-party traffic control services, to prevent any harm to our platform. We conduct periodic reviews of our technology platform identifying and correcting problems that may undermine our system security.

Our stable IT infrastructure is hosted by two separate cloud service providers. We achieve redundancy and reliability of our network through a real-time multi-layer data backup system. Our platform adopts modular architecture that consists of multiple connected components, each of which can be separately upgraded and replaced without compromising the functioning of other components. This makes our platform both highly reliable and scalable.

Our platform is scalable and can be easily expanded as data storage requirements and user visits increase. In addition, load balancing technology helps us improve distribution of workloads across multiple computing components, optimizing resource utilization and minimizing response time.

Environmental, Social and Governance (ESG) Initiatives

We are committed to corporate social responsibility and meeting society's changing needs despite the recent challenging economic environment. We are committed to supporting and participating in socially responsible projects that align with our core values and mission, and to extend the benefits of our products and services through our technology-driven platform to the community at large.

In response to the recurrence of coronavirus (COVID-19), we have taken a series of initiatives , including :

- 1 Clinic has provided approximately 520,000 free medical consultations in 2021.
- In February 2021, we provided pharmacies in Covid-affected northern regions (i.e., Jilin, Heilongjiang, Liaoning and Hebei Provinces) with PPEs and other related services.
- In June 2021, we donated equipment, including surgical masks and disinfectants, through various charities in Guangzhou City.
- In July 2021, 1 Clinic provided free online consultations to patients impacted by the severe flooding in Henan Province.
- 1 Clinic has partnered with the People's Hospital of Wenjiang District, Chengdu City, to launch an initiative aimed at the prevention and treatment of hydatid disease. Partnership includes using our technologies to build a doctor-patient consultation platform to help doctors provide convenient, high quality medical services for ethnic Tibetans in Seda County, Sichuan Province.

In aspect of the consumer safety, we launched a collection program for expired medication to ensure safe disposal.

Meanwhile, we also adopted a series of environment-friendly measures aiming to reducing carbon emissions, including:

- Proactive advocacy of the environmental philosophy of green lifestyles.
- Paperless operations in goods arrival, stocking, picking, stock checking and other processes in the fulfillment centers.

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- Substantial reduction in the use of non-degradable consumables in the transportation and packaging process.

Sales and Marketing

Our marketing and promotion strategy is to build brand recognition, increase customer traffic, attract new customers, build strong customer loyalty and develop incremental revenue opportunities.

We employ a variety of methods to attract potential consumers. Generally, we expand our user base on our marketplace through search engines, social media and word-of-mouth referrals. We offer incentives to new consumers and pharmacy customers who make purchases for the first time on our platform. We also offer flash sales and brand promotion events on our website and mobile application to engage with existing consumers in an effort to increase retention and repurchases. Our principal marketing programs include advertising our company and our solutions through our mobile platform and other media.

We acquire pharmacy customers primarily through our effective on-the-ground sales operation to allow rapid expansion of our wholesale business. We have full-time employees who visit independent pharmacies, pharmacy chains and in-house pharmacies within clinics and private hospitals to promote our online wholesale pharmacy and our inventory management services. We also hire independent contractors who work for us on a commission-basis to promote our products and services to pharmacies through our “City Partners” program. We also coordinate market development and promotion efforts for our pharmacy customers, which may include flash sales, seasonal sales discounts and rebates.

Competition

We believe our business model is unique and our services encompass the entire pharmaceutical value chain. We believe there are no comparable companies that directly compete with us. However, we face intense competition in certain business segments and verticals:

- we compete against other pharmaceutical retail companies including traditional offline pharmacies and online platforms, such as Ali Health and JD.com; and
- we also face competition from numerous B2B platforms and traditional pharmaceutical distributors.

We believe that our ability to compete effectively depends on many factors, including the variety of our products, our pricing competitiveness, user experience on our platform, our technological leadership, effectiveness of our risk management, our partnership with third parties, our marketing and selling efforts and the strength and reputation of our brands.

Furthermore, as our business continues to grow rapidly, we face significant competition for highly skilled personnel, including management, engineers, product managers and risk management personnel. The success of our growth strategy depends in part on our ability to retain existing personnel and add additional highly skilled employees. We believe that our early mover advantage and leading market position help us to compete efficiently against our competitors.

Intellectual Property

We rely on a combination of copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. We have registered 30 software copyrights with the PRC National Copyright Administration. We have 32 registered domain names, including 111.com.cn and yaoex.com. As of December 31, 2021, we had 281 registered trademarks, including our “1药网” trademark. As of the same date, we had 19 authorized patents in the areas of digital health, big data analytics, and SMART supply chain technology with the China National Intellectual Property Administration.

Insurance

We maintain property insurance policies covering certain equipment and other property that are essential to our business operations to safeguard against risks and unexpected events. We also provide social security insurance including pension, medical insurance, unemployment insurance, maternity insurance, on-the-job injury insurance and housing fund plans through a PRC government-mandated benefit contribution plan for our employees. We maintain product liability insurance. We also maintain

professional malpractice insurance for our in-house licensed medical practitioners and some of our external doctors. We do not maintain business interruption insurance. We consider our insurance coverage to be sufficient for our business operations in China.

Regulations

This section sets forth a summary of the most significant rules and regulations that affect our business activities in China.

Regulation Relating to Foreign Investment

Investment in the PRC conducted by foreign investors and foreign-owned enterprises shall comply with the Guidance Catalogue of Industries for Foreign Investment, or the Catalogue, which was first issued in 1995 and amended from time to time. The current effective Catalogue was promulgated by the MOFCOM and the NDRC in June 2017 and became effective in July 2017, and contains specific provisions guiding market access of foreign capital and stipulates in detail the areas of entry pertaining to the categories of encouraged foreign-invested industries, restricted foreign-invested industries and prohibited foreign-invested industries. The latter two categories are included in the negative list, which was first introduced into the Catalogue in 2017, and listed, in a unified manner, the restrictive measures for the entry of foreign investment. On December 27, 2021 and December 27, 2020, the MOFCOM and the NDRC jointly promulgated the Special Administrative Measures for Access of Foreign Investment (Negative List) (2021 Edition) and the Catalog of Industries for Encouraged Foreign Investment (2020 Edition) respectively, to replace the former negative lists and the Catalogue, which took effect on January 1, 2022 and January 27, 2021 respectively. Any industry not listed in the Catalogue and the Negative List is a permitted industry and generally open to foreign investment unless specifically prohibited or restricted by PRC laws and regulations. According to the Negative List, value-added telecommunications services (with the proportion of foreign investment not exceeding 50%, except for e-commerce) and medical institutions (limited to sino-foreign equity joint venture or sino-foreign cooperative joint venture) are restricted for foreign investment. 1 Pharmacy Technology, our PRC subsidiary, is a foreign-invested enterprise and conducts technical services and consultation and sale of goods that falls in permitted industries for foreign investment. Wuhan Central China, our 70% owned PRC subsidiary, is an entity invested by a foreign-invested enterprise and conducts online B2B pharmaceutical e-commerce business which is classified as a type of value-added telecommunications services. It falls in the restricted foreign-invested industry but is not subject to the 50% foreign investment restriction. Our subsidiary Yihao Pharmaceutical Chain operates e-commerce business, which is classified as a type of value-added telecommunications services that falls within the restricted foreign-invested industry but is not subject to the 50% foreign investment restriction. Chengdu Yizhen Internet Hospital Co., Ltd., one of our PRC subsidiaries, operates internet hospital, which falls within the restricted foreign-invested industry. In March 2012, Sichuan Provincial Department of Health and Sichuan Provincial Department of Commerce promulgated the Administrative Measures of Sichuan Province on Sino-foreign Joint Venture and Cooperative Medical Institutions, which requires that the equity proportion or interest of Chinese investors in a joint venture or cooperative medical institution shall not be less than 10%. As of the date of this annual report, the equity proportion of Chinese investors in Chengdu Yizhen Internet Hospital Co., Ltd. is no less than 10%.

In September 2016, the SCNPC, passed a decision in connection with the revision of four laws, including the trio of laws regulating foreign investment in China, which became effective in October 2016. According to this decision, establishment of a foreign-invested enterprise, or the FIE, in a sector not subject to special entry administrative measures will be simplified by going through government filing instead of a government approval process, which applies to its establishment, separation, merger or other major modifications and operation duration and extension; but the special entry administrative measures are to be separately promulgated or approved to be promulgated by the State Council. According to a notice issued by the NDRC and the MOFCOM in October 2016, the special entry administrative measures shall be applicable and implemented to the restricted foreign-invested industries, prohibited foreign-invested industries and encouraged foreign-invested industries which have requirements as to shareholding and qualifications of senior management stipulated in the then-effective Catalogue.

In March 2019, a new draft of Foreign Investment Law was submitted to the National People's Congress for review and was approved on March 15, 2019, which has come into effect on January 1, 2020 and replaced the trio of laws regulating foreign investment in China. Its implementation of regulations promulgated by the State Council in December 2019 also came into effect on January 1, 2020. Under new Foreign Investment Law, foreign investment refers to investment activity directly or indirectly conducted by foreign natural persons, enterprises or other organizations, including the following circumstances: (i) a foreign investor establishes a foreign-funded enterprise within the territory of China, independently or jointly with any other investor; (ii) a foreign investor acquires shares, equities, property shares or any other similar rights and interests of an enterprise within the territory of China; (iii) a foreign investor makes investment to initiate a new project within the territory of China, independently or jointly with any other investor; and (iv) a foreign investor makes investment in any other way stipulated by laws, administrative regulations or provisions of the State Council. Foreign investors shall not invest in any field forbidden by the negative list for access of foreign investment and shall conform to the investment conditions stipulated under the negative list for any field restricted by the negative list. Fields not included in the negative list shall be managed under the principle that domestic investment and foreign investment shall be treated uniformly. In addition, a foreign investment information reporting system shall be established and foreign investors or foreign-funded enterprises shall submit the investment information to competent departments for commerce through the enterprise registration system and the enterprise credit information publicity system.

Our PRC subsidiary, 1 Pharmacy Technology, as a foreign-invested enterprise, is not subject to the special entry administrative measures and has filed with the competent commerce authority for its establishment and modification as requested. Certain of our PRC subsidiaries, including Wuhan Central China, Yihao Pharmaceutical Chain and Chengdu Yizhen Internet Hospital Co., Ltd., are entities that are directly or indirectly invested by a foreign-invested enterprise and conduct business falling within the restricted foreign-invested industry. As of the date of this annual report, Wuhan Central China and Chengdu Yizhen Internet Hospital Co., Ltd. have obtained the approval from, and made filing with, the competent commerce authority. Yihao Pharmaceutical Chain is in the process of cancelling its ICP/EDI License and reapplying for the EDI License due to the termination of the VIE structure which caused it to become a foreign-owned enterprise.

In August 2006, six PRC regulatory agencies, including the MOFCOM, jointly adopted the M&A Rules, which became effective in September 2006 and were amended in 2009. The M&A Rules also establish procedures and requirements that could make certain acquisitions of PRC companies by foreign investors more time-consuming and complex, including requirements in some instances that MOFCOM be notified in advance of any change-of-control transaction in which a foreign investor takes control of a PRC domestic enterprise. In addition, according to the Notice on Establishing the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors issued by the General Office of the State Council in February 2011, the Rules on Implementation of Security Review System for the Merger and Acquisition of Domestic Enterprises by Foreign Investors issued by the MOFCOM in August 2011, mergers and acquisitions by foreign investors that raise "national defense and security" concerns and mergers and acquisitions through which foreign investors may acquire de facto control over domestic enterprises that raise "national security" concerns are subject to strict review by the MOFCOM, and the regulations prohibit any activities attempting to bypass such security review, including by structuring the transaction through a proxy or contractual control arrangement.

In December 2020, the NDRC and the MOFCOM further promulgated the Foreign Investment Security Review Measures, which took effect on January 18, 2021. These measures require direct or indirect investment by foreign investors in PRC companies engaged in military-related or certain other industries be subject to security review before consummation of any such investment. "Certain other industries" refer to, among others, important transportation services, important culture products and services, important information technology and internet products and services, and important finance services that are crucial to national security.

Regulation Relating to Value-added Telecommunications Services

Telecommunications Regulations

The Telecommunications Regulations of the People's Republic of China, or the Telecom Regulations, promulgated in September 2000 and amended in July 2014 and February 2016 respectively, are the primary PRC laws governing telecommunication services, and set out the general framework for the provision of telecommunication services by domestic PRC companies. The Telecom Regulations require that telecommunications service providers obtain operating licenses prior to commencing operations. The Telecom Regulations draw a distinction between “basic telecommunications services” and “value-added telecommunications services.” The catalogue of Telecommunications Business, or the Telecom Catalogue, issued as an attachment to the Telecom Regulations, identifies information services and online data and transaction processing services as value-added telecommunications services.

In July 2017, the MIIT issued the revised Measures on the Administration of Telecommunications Business Operating Permits, or the Telecom License Measures, which became effective in September 2017, to supplement the Telecom Regulations. The Telecom License Measures require that an operator of value-added telecommunications services obtain a value-added telecommunications business operating license, from the MIIT or its provincial level counterparts. The term of a license for value-added telecommunication business is five years and subject to annual inspection.

Foreign Investment in Value-Added Telecommunications

Foreign direct investment in telecommunications companies in China is also regulated by the Regulations for the Administration of Foreign-Invested Telecommunications Enterprises, or the FITE Regulations, which were issued by the State Council in December 2001 and amended in September 2008 and February 2016, respectively. The FITE Regulations stipulate that a foreign invested telecommunications enterprise in the PRC, or the FITE, must be established as a sino-foreign equity joint venture for operations in the PRC. Under the FITE Regulations and in accordance with WTO-related agreements, the foreign party investing in a FITE engaging in value-added telecommunications services may hold up to 50% of the equity interests of the FITE. In addition, the major foreign party to be the shareholder of the FITE must satisfy a number of stringent performance and operational experience requirements, including demonstrating a good track record and experience in operating a value-added telecommunications business. The FITE that meets these requirements must obtain approvals from the MIIT and the MOFCOM or its counterparts, which retain considerable discretion in granting approvals. Furthermore, the foreign party investing in e-commerce business, as a type of value-added telecommunication services, has been allowed to hold up to 100% of the equity interests of the FITE based on the Notice of the Ministry of Industry and Information Technology on Removing the Restrictions on Foreign Equity Ratios in Online Data Processing and Transaction Processing (Operating E-commerce) Business issued on in June 2015 and the current effective Telecom Catalogue.

In July 2006, the Ministry of Information Industry, which was restructured and integrated into the MIIT, promulgated the Notice of the Ministry of Information Industry on Intensifying the Administration of Foreign Investment in Value-added Telecommunications Services, or the MII Notice, which reiterates certain requirements of the FITE Regulations and strengthens the administration by the MII. Under the MII Notice, if a foreign investor intends to invest in a PRC value-added telecommunications business, the FITE must be established to apply for a telecommunications business license applicable to the business. In addition, a domestic company that holds a license for the provision of value-added telecommunications services is prohibited from leasing, transferring or selling the license to foreign investors in any form, and from providing any assistance, including providing resources, sites or facilities, to foreign investors to conduct value-added telecommunications businesses illegally in China. Trademarks and domain names that are used in the provision of value-added telecommunications services must be owned by the license holder or its shareholders. The MII Notice also requires that each value-added telecommunications services license holder have appropriate facilities for its approved business operations and to maintain such facilities in the business regions covered by its license.

Yihao Pharmaceutical Chain owns the domain names, trademarks, and facilities that are necessary to operate its telecommunication business. Yihao Pharmaceutical Chain operates e-commerce business, which falls within the scope of online data processing and transaction processing (operating e-commerce), and therefore foreign investors are allowed to hold 100% of the equity of these two entities. We terminated the contractual arrangements between 1 Pharmacy Technology and each of the previous variable interest entities (i.e., Yihao Pharmacy, Yihao Pharmaceutical Chain and Shanghai Yaowang) to reduce the legal uncertainties associated with the VIE structure.

Internet Information Services and Online Data Processing and Transaction Processing Business

In September 2000, the State Council promulgated the Measures for the Administration of Internet Information Services, or the ICP Measures, as amended in 2011. Under the ICP Measures, the internet information services are divided into commercial internet information services and non-commercial internet services. The operators of non-commercial internet information services must file with relevant governmental authorities and operators of commercial internet information services in China must obtain a license for internet information provision, or ICP license, from the relevant governmental authorities, and the provision of particular information services, such as news, publishing, education, healthcare, medicine and medical device, and must also comply with relevant laws and regulations and obtain the approval from competent governmental authorities.

Pursuant to the Telecommunications Regulations and the Telecom Catalogue, an e-commerce operator shall obtain a license for value-added telecommunications services with the specification of online data processing and transaction processing business (e-commerce only) (the “EDI License”) from appropriate telecommunications authorities. Wuhan Central China has obtained the EDI License to operate e-commerce business and Yihao Pharmaceutical Chain is reapplying for the EDI License.

Mobile Internet Applications Information Services

In June 2016, the CAC promulgated the APP Provisions, which became effective in August 2016. Under the APP Provisions, mobile application providers and application store service providers are prohibited from engaging in any activity that may endanger national security, disturb the social order, or infringe the legal rights of third parties, and may not produce, copy, issue or disseminate through internet mobile applications any content prohibited by laws and regulations. The APP Provisions also require application providers to procure relevant approval to provide services through such applications and require application store service providers to register with local branches of the CAC within 30 days after they start providing application store services.

Regulations Relating to Pharmaceutical Operation and Service

Pharmaceutical Operation

In September 1984, the SCNPC promulgated the Drug Administration Law, which was amended in 2001, 2013, 2015 and 2019 respectively to regulate all entities or individuals engaging in research, manufacture, operation, use, supervision and management of drugs within the PRC. According to the Drug Administration Law, no pharmaceutical operation, including pharmaceutical wholesale and pharmaceutical retail business, is permitted without obtaining the Pharmaceutical Operation License. The Implementation Rules for the Drug Administration Law, was promulgated by the State Council in August 2002 and amended in 2016 and 2019, which emphasized the detailed implementation rules of drugs administration. The CFDA promulgated the Measures for the Administration of Pharmaceutical Operation License in February 2004 as amended in 2017, which stipulate the procedures for applying the Pharmaceutical Operation License and the requirements and qualifications for pharmaceutical wholesalers or pharmaceutical retailers with respect to their management system, personnel, facilities and etc. The valid term of the Pharmaceutical Operation License is five years and shall be renewed six months prior to its expiration date.

According to the Measures on Prescription Drugs and OTC Drugs Classification Management and the Interim Provisions on the Circulation of Prescription and OTC Drugs (Trial), which were both promulgated by the State Drug Administration, which was restructured and integrated into the CFDA, in 1999 and became effective in January 2000, drugs are divided into prescription drugs and over-the-counter drugs, or OTC drugs. For prescription drugs, the dispensing, purchase and use can only be based on the prescription issued by the certified medical practitioner or certified medical assistant practitioner. In addition, the prescription drugs can only be advertised and promoted in professional medical magazines. OTC drugs, on the other hand, are further divided into Class A and Class B and they both can be purchased and used without a prescription and promoted in public upon approval by the relevant governmental authorities. The pharmaceutical wholesale enterprises distributing prescription drugs and/or OTC drugs, as well as pharmaceutical retail enterprises selling prescription drugs and/or Class A OTC drugs are required to obtain the Pharmaceutical Operation License.

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According to the Administrative Measures for the Supervision and Administration of Circulation of Pharmaceuticals, promulgated by the CFDA in January 2007 and effective in May 2007, pharmaceutical manufacture and operation enterprises and medical institutions shall be responsible for the quality of pharmaceuticals they manufacture, provide or use. The operation of prescription drugs is highly regulated under these rules. Prescription drugs may not be sold by pharmaceutical retail enterprises without valid prescriptions and an enterprise in violation of such restriction will be instructed to rectify any violation, given a disciplinary warning, and/or imposed a fine of no more than RMB1,000. In addition, a pharmaceutical manufacture or operation enterprise shall not sell prescription drugs directly to the public by post or over internet, and the enterprise in violation of such restriction shall be instructed to rectify, given a disciplinary warning, and fined the lesser of (i) two times the value of the pharmaceuticals sold and (ii) RMB 30,000. The Drug Administration Law abolishes the restriction on online sale of prescription drugs and adopts the principle of keeping online and offline sales consistent, which allows the qualified pharmaceutical enterprise to conduct online sale of drugs (including prescription drugs, but not certain special controlled drugs). In addition, the entity that operates a third-party online drug transaction platform shall be filed with relevant authority for drugs supervision and administration and responsible to examine the qualifications of the drug marketing permit holders and drug operation enterprises applying to operate on its platform, ensure that they meet legal requirements, and manage the drug operation behaviors occurring on the platform. However, as of the date of this annual report, none of the regulations or implementation rules regulating online drug sales have yet been promulgated and implemented, which may further introduce and impose certain conditions and restrictions to the online sale of drugs. Furthermore, the Administrative Standard of Pharmaceutical Operating Quality, promulgated by the CFDA in April 2000 and amended in 2012, 2015 and 2016, respectively, and the Administrative Measures for Identification of Pharmaceutical Operating Quality Administrative Standards, promulgated by the CFDA in April 2003, which was replaced by the Administrative Measures for Drug Inspection (Trial) promulgated by the NMPA and became effective in May 2021, the pharmaceutical operation enterprise shall take effective quality control measures over the process of procurement, storage, transportation and sale of drugs in order to ensure their quality and the drug supervision and administration authorities shall have the right to inspect the compliance of relevant entities with laws and regulations in production, operation and use of drugs, the implementation of relevant quality management practice and the drug standards.

Medical Devices Operation

According to the Regulations on the Supervision and Administration of Medical Devices, which was promulgated by the State Council in January 2000 and amended in 2014, 2017 and 2021, respectively, and the Supervision and Management Measures on Medical Devices Operation, which was promulgated by the CFDA in July 2014 and amended in 2017, business operations of medical devices are regulated based on the degree of risks involving the medical devices, which are divided into three categories. Operation of Class I medical devices does not require a license or record-filing, while operations of Class II medical devices and Class III medical devices are subject to record-filing and licensing requirements, respectively. An entity engaging in the operation of medical devices shall meet certain requirements with respect to its management system, personnel, facilities etc., and shall apply for approval to operate Class III medical devices and make record-filing with relevant governmental authority to operate Class II medical devices. The valid term of medical devices operation permit is five years.

Regulations Relating to Online Operation of Drugs and Medical Devices

Internet Drug Information Service

The Administrative Measures on Internet Drug Information Service, or Internet Drug Measures, was promulgated by the CFDA in July 2004 and amended in 2017, pursuant to which the internet drug information services is to provide drug (including medical device) information services to online users, which is divided into commercial internet drug information services and non-commercial internet drug information services. The website operator that provides drugs (including medical devices) information services must obtain an Internet Drug Information Service Qualification Certificate from the competent counterpart of the CFDA. The valid term for an Internet Drug Information Service Qualification Certificate is five years and may be renewed at least six months prior to its expiration date upon a re-examination by the relevant governmental authorities.

Furthermore, as requested by Internet Drug Measures, the information relating to drugs shall be accurate and scientific in nature, and its provision shall comply with the relevant laws and regulations. No product information of stupefiant, psychotropic drugs, medicinal toxic drugs, radiopharmaceutical, detoxification drugs and pharmaceutics made by medical institutes shall be distributed on the website. In addition, advertisements relating to drugs (including medical devices) shall be approved by the NMPA or its competent counterparts.

Internet Drug Transaction Services

The Interim Provisions on the Examination and Approval of Internet Drug Transaction Services, or Interim Portions of Internet Drug Transaction, were promulgated by the CFDA in September 2005 and became effective in December 2005, and regulate transaction of drugs (including medical devices and packing materials and containers that are in direct contact with drugs) over internet, including the provision of transaction services among pharmaceutical manufacturers, pharmaceutical operation enterprises and medical institutes, the services provided by pharmaceutical manufacturers and pharmaceutical wholesale enterprises to other third parties via their own websites and services provided by pharmaceutical retail chain enterprises to individual consumers. According to Interim Portions of Internet Drug Transaction enterprises engaging in providing drug transaction services over the internet must obtain an Internet Drug Transaction Qualification Certificate. Such certificates have a term of five years and have three types: A certificate, B certificate and C certificate. They are only issued to three kinds of enterprises: (i) enterprises that provide drug transaction services to pharmaceutical manufacturers, pharmaceutical operation enterprises and medical institutions, but do not participate in pharmaceutical manufacture and operation and do not own, have no property relationship or other economic interest with the administrative organizations, medical institutions or pharmaceutical manufacture and operation enterprises; (ii) pharmaceutical manufacturers and pharmaceutical wholesale enterprises that deal with other third-party enterprises via their own websites; (iii) the pharmaceutical retail chain enterprises that provide OTC drug transaction services for individual consumers via the internet.

However, according to the Decision on the Cancellation of the Third Batch of Items Subject to Administrative Permission by Local Governments Designated by the Central Government, promulgated by the State Council in January 2017, except for third-party platforms, all approval of internet drug transaction service enterprises implemented by counterparts of CFDA at the provincial level are cancelled. In April 2017, the General Office of the CFDA promulgated a notice on implementing the above mentioned decision, pursuant to which pharmaceutical manufacture enterprises and pharmaceutical wholesale enterprises may carry out internet drug (including medical device) transactions with other enterprises through their own websites, but shall not provide internet drug (including medical device) transaction services to individual consumers. In addition, pharmaceutical retail chain enterprises may provide internet drug (including medical device) transaction services to individual consumers, but they shall not exceed the business scope permitted by license and filings and display information of prescription drugs on related transaction webpages, or sell prescription drugs or the OTC drugs under special administrative requirements; as indicated in such decision, the CFDA will promulgate subsequently the relevant rules on supervision of internet drug (including medical device) transaction.

Furthermore, according to the Decision on the Cancellation of Various Items Subject to Administrative Permission promulgated by the State Council in September 2017, the enterprises engaging in internet drug transaction service as a third-party platform shall no longer be subject to the examination and approval of the CFDA before carrying out such business. In November 2017 the General Office of the CFDA promulgated a Notice on Strengthening the Administration and Supervision of Internet Drug and Medical Devices Transaction, which specify the approval to conduct internet drug transaction service as the third-party platform is cancelled, but enterprises carrying out internet drug (including medical) transaction services shall establish a comprehensive supervision system in general and also request local counterparts of CFDA to implement day-to-day supervision and examination with respect to qualification access examination, products inspection, storage of transaction data and legal liabilities etc.

Online Sales of Drugs and Medical Device

Under PRC laws and regulations, the drugs and medical devices are allowed to be sold online in general except the prescription drugs that cannot be sold by pharmaceutical manufacture and operating enterprise or medical institution directly to the public by post or via internet.

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In November 2017, the CFDA released a draft of the Administrative Measures for Supervision and Regulation of Online Drug Sales for public consultation, which aims to regulate online drug sales in the PRC. In February 2018 and November 2020, the CFDA also released two drafts for online drug sales for public consultation. All of the drafts stipulate that sellers and online platforms engaging in this business shall obtain relevant certificates or satisfy relevant conditions to guarantee the safety and quality of the drugs. Furthermore, according to the latest draft, the platform shall make record-filing with the counterparts of the NMPA at provincial level. In particular, only drug retail enterprises who satisfy the conditions for online sales of prescription drugs are allowed to display prescription drugs information to the public, and shall expressly indicate that the prescription drugs must be bought and used with prescriptions under the guidance of licensed pharmacist and other risk warning information. The newly revised Drug Administration Law in 2019 abolishes the restrictions on online sale of prescription drugs and only prohibits special types of drugs to be sold via the internet, including vaccines, blood products, anesthesia and psychiatric drugs, toxic drugs for medical use, radiative drugs, pharmaceutical precursor chemicals or other drugs subject to special administration. This new law adopts the principle of keeping the online and offline sales consistent, under which the entity conducting online sale of drug shall possess a valid license for medicine operation and the third-party platform provider shall examine the qualifications of the drug marketing permit holders and drug operation enterprises applying to operate on its platform, ensure that they meet legal requirements, and manage the drug operation behaviors occurring on the platform. In November 2021, the NMPA released a draft of the Administrative Measures for the Supervision and Administration of Pharmaceutical Operations and Use, or the Draft Pharmaceutical Operations and Use Measures, which stipulates that drugs operation enterprises selling drugs online shall abide by the relevant provisions of the Drug Administration Law and the relevant provisions on supervision and administration of online sales of drugs. However, as of the date of this annual report, the Draft Pharmaceutical Operations and Use Measures has yet to come into effect. It is uncertain when it will be signed into law and whether the final version will deviate substantially from the draft. In addition, as of the date of this annual report, none of the regulations or implementation rules regulating online drug sales have yet been promulgated and implemented, which may further introduce and impose certain conditions and restrictions to the online sale of drugs, including but not limited to the transaction method, qualifications and type of drugs, and there are substantial uncertainties with respect to their enactment timetable and final provisions.

In December 2017, the CFDA promulgated the Administration and Supervision Measures of Online Sales of Medical Devices, or the Online Medical Devices Sales Measures, which became effective in March 2018. According to the Online Medical Devices Sales Measures, enterprises engaged in online sales of medical devices must be medical device manufacture and operation enterprises with medical devices production licenses or operation licenses or being filed for record in accordance with laws, unless such licenses or record-filing is not required by laws and regulations, and the third-party platform for provision of online medical devices transaction services shall obtain an Internet Drug Information Services Qualification License. Either enterprises for online sales of medical devices or enterprises for provision of medical devices online transaction services shall take technical measures to ensure the data and materials of medical devices online sales are authentic, completed and retrospective, for example the records of sale information of medical devices shall be kept for two years after the valid period of the medical devices, and for no less than five years in case of no valid period, or be kept permanently in case of implanted medical devices. In March 2021, the NMPA released the Supervision and Management Measures on Medical Devices Operation (Revised Draft for Comment), according to which the registrant, filing party and operation enterprise of medical device and who engage in online sale of medical device shall apply for license or filing in accordance with this measures and shall inform relevant drug regulatory authority of the name, domain name, IP address of the websites and other relevant information, with an exception of operations of Class I medical devices or Class II medical devices which are exempted from operation filing. As of the date of this annual report, this revised draft has yet to come into effect.

Regulations Relating to Online Trading

The Measures for the Supervision and Administration of Online Trading promulgated by the SAMR in March 2021, or the Online Trading Measures, which became effective since May 2021 and replaced the Administrative Measures for Online Trading, or Online Trading Measures promulgated by the SAIC in January 2014, stipulates the obligations of online trading operators, including the online trading platform operators, operators within the platform, self-built website operators and online trading operators that carry out online trading activities through other network services. Social networking, live streaming or other network services providers provide online business premises, commodity browsing, order generation, online payment or other online trading platform services for operators shall fulfill the obligations of online trading platform operators in accordance with the law. The MOFCOM promulgated the Provisions on the Procedures for Formulating Transaction Rules of Third Party Online Retail Platforms (Trial) in December 2014, which became effective in April 2015, to guide and regulate the formulation, revision and enforcement of transaction rules by online retail third-party platforms operators. These measures impose more stringent requirements and obligations on third-party platform operators. For example, third-party platform operators are obligated to make public and file their transaction rules with MOFCOM or their respective provincial counterparts, examine and register the legal status of each third-party merchant selling products or services on their platforms and display on a prominent location on a merchant's webpage the information stated in the merchant's business license or a link to its business license. Where third-party platform operators also act as online distributors, these third-party platform operators must make a clear distinction between their online direct sales and sales of third-party merchant products on their third-party platforms. Furthermore, in August 2018, the SCNPC promulgated the E-Commerce Law, which took effect on January 1, 2019 and aims to regulate the e-commerce activities conducted within the territory of the PRC. According to the E-Commerce Law, e-commerce operators shall comply with the principles of voluntariness, equality, fairness, and good faith, abide by laws, observe business ethics, equally participate in market competition. It further strengthened the performing obligations of e-commerce operators regarding to the protection of consumers' rights and interests, environmental protection, intellectual property protection, and the protection of cyberspace safety and personal information, and also emphasized the commitment by e-commerce operators over the quality of products and services.

After the issuance of Online Trading Measures, the SAIC has issued a number of guidelines and implementing rules aimed at adding greater specificity to these regulations and continues to consider and issue guidelines and implementing rules in this industry. For example, three PRC governmental authorities (the Ministry of Finance of the People's Republic of China, or the MOF, General Administration of Customs, or the GAC, and the STA) issued the New Cross-Border E-commerce Retail Imports Tax Notice in March 2016, which became effective in April 8, 2016 and was amended in November 2018, to regulate cross-border e-commerce trading and introduced the concept of the cross-border e-commerce retail importation goods inventory, or the Cross-Border E-Commerce Goods Inventory, which has been issued and updated by the three authorities together with other relevant authorities from time to time. Two batches of the Cross-Border E-Commerce Goods Inventory and the Cross-Border E-Commerce Goods Inventory (2018 Edition) issued in April 2016 and November 2018 have been replaced by the Cross-Border E-Commerce Goods Inventory (2019 Edition) issued in December 2019 and the Notice of Relevant Matters on Implementation of New Cross-Border E-Commerce Retail Importation Supervision and Administration Requirements has been issued by the GAC in May 2016 to further implement the rules. According to the Notice of Relevant Work on improving Cross-Border E-Commerce Retail Importation Supervision and Administration issued in November 2018, retail imported goods on cross-border e-commerce platforms will be temporarily treated as personal items which are not subject to stricter regulations and higher tax rates applicable to normal imported goods in 37 cross-border e-commerce trial areas.

Regulations Relating to the Medical Industry

Medical Institution

The Administrative Regulations on Medical Institutions was promulgated by the State Council in February 1994 and amended in 2016 to regulate all medical institutions, such as hospitals, health centers, sanatoriums, out-patient departments, clinics and health posts (rooms) as well as first-aid stations. The establishment of medical institutions by the entity or individual shall be subject to examination and approval of the health administrative authorities at the county level or above and medical institutions must obtain the approval certificate to establish the medical institution. Furthermore, the medical institution shall also register with competent health administrative authorities for practice and operation, and obtain the License for Practicing of Medical Institutions after examination by competent health administrative authorities. Chengdu Yizhen Internet Hospital Co., Ltd. has obtained a License for Practicing of Medical Institutions, and Guangdong Yihao Pharmaceutical Chain Co., Ltd. Dongshan Branch Traditional Chinese Medicine Clinic has obtained Licenses for Practicing of Medical Institution only for traditional Chinese medicine and internal medicine.

According to the Notice on Issuance of the Opinions on the Pilot of Promoting Clinics Development issued by the MOF, the MOHRSS and the NHSA in April 2019, the pilot program of promoting clinic development was suggested be implemented in 10 cities, where the establishment of such clinics would not be subject to examination and approval but filing with relevant health administrative authorities. According to the Decision of the State Council on Amending and Repealing Some Administrative Regulations, since May 2022, all clinics will be allowed to practice after completing filing procedures instead of obtaining the License for Practicing of Medical Institutions.

Internet Medical Services

On May 1, 2009, the Ministry of Health of the People's Republic of China, which was restructured and integrated into the NHFPC and subsequently to the NHC, promulgated the Administrative Measures on Internet Medical and Healthcare Information Services to regulate the business relating to providing online medical and healthcare information; but such measures were abolished in January 2016.

In August 2014, the NHFPC issued an opinion to promote medical institution's remote diagnosis and treatment services. Under this opinion, the medical institutions shall possess qualified personnel, technology, facilities to carry out remote diagnosis and treatment services, and shall also satisfy certain requirements. Non-medical institutions are prohibited from providing remote diagnosis and treatment services.

In July 2015, the State Council issued a guiding opinion to promote activities of the concept of "Internet +", including popularizing the model of online medical services to develop the medical services via internet and support medical information sharing service platform. In December 2016, the State Council promulgated the 13th Five-Year sanitation and health planning, which suggests to comprehensively implement "Internet +" Healthcare service, and encourages the establishment of regional remote medical service platform and promotes the vertical flow of high quality medical resources.

According to an official reply to a proposal put forward in the fourth meeting of the twelfth committee of the Chinese People's Political Consultative Conference in June 2016 and released in November 2016 on the website of NHFPC, it indicates that no online diagnosis and treatment shall be allowed except for remote diagnosis and treatment; but it allows online health consultation provided by practitioners or other personnel via network platform operated by internet companies and medical consultation made by practitioners without provision of written diagnosis and prescription and other implementation of doctors' advice. As indicated in another official reply to a recommendation made in the fifth meeting of China's twelfth National People's Congress issued in December 2017 by the NHFPC, the administration measures for internet diagnosis and treatment are under research and formulation, which aims to specify the business scope of internet diagnosis and treatment, information security, patient privacy protection, supervision and legal liabilities.

In April, 2018, the General Office of State Council promulgated the opinions concerning development of "internet + healthcare" that specifies that both medical institutions and qualified enterprises could set up and operate "internet hospital" to offer approved services and the prescription drugs for common and chronic disease prescribed by pharmacist could be delivered by third parties designated by pharmaceutical operating entities, which would allow the pharmaceutical enterprise to sell the prescription drugs to individual by mail. In July 2018, the NHC and the State Administration of Traditional Chinese Medicine, or the SATCM, jointly promulgated the Notice of Carrying Out In-depth Activities for the Benefit of the People regarding "Internet + Healthcare", which further specified that after e-prescriptions have been approved by pharmacists, pharmaceutical enterprises can designate qualified third party couriers to deliver the prescription drugs.

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In July 2018, the NHC and the SATCM issued the Administrative Measures for Online Diagnosis and Treatment (Trial), the Administrative Measures for Internet Hospitals (Trial), or the Internet Hospital Administrative Measures and the Administrative Standards for Remote Diagnosis (Trial). According to these measures and standards, internet hospitals including the internet hospitals used as second name of a physical medical institution and the internet hospitals established independently while relying on a physical medical institution, and are subject to access restrictions. The application for establishment of internet hospitals shall be submitted to the registration department of the physical medical institution. The Internet Hospital Administrative Measures also provide the basic standards for internet hospitals, including the requirements for diagnosis subjects, department settings, staffs, buildings and facilities, rules and regulations. In October 2021, the NHC released a draft of the Detailed Rules on Supervision and Administration of Internet Diagnosis and Treatment, which provides detailed implementation rules of supervision and administration on the medical institutions, practitioners, operations and quality and safety of internet diagnosis and treatment. As of the date of this annual report, this draft has yet to come into effect.

In June 2019, a Notice on Issuance of the Opinions on Promotion of the Sustained, Healthy and Normalized Development of Social Medical was issued, which supports social medical to develop “Internet + Healthcare”, encourages medical institutions to use internet and other information technology in expanding the medical service space and building an integrated medical service model, and supports medical and healthcare institutions and qualified third-party institutions to build internet information platform and provide remote medical services, healthcare consultation and health management services.

In 2020, the NHC, together with relevant authority, promulgated a series of policies such as the Circular on Further Promoting the Development and Standardized Administration of Online Medical Services, the Guiding Opinions on Promoting the “Internet” Medical Insurance Services during the Period of COVID-19 Prevention and Control, the Circular Relating to Internet Diagnosis and Treatment Consultation Services in COVID-19 Prevention and Control, to further promote the integrated development of internet technologies and medical services, facilitate medical services seeking and drugs purchasing by insured people, reduce the risk of crowd gathering and cross-infection, provide high-quality and convenient medical consultation services for broad masses by using the advantages of “internet + Healthcare”.

In July 2021, the NHSA promulgated the Opinions on Optimizing the Convenient Services in Medical Insurance Sector, to promote standardized and normalized construction of healthcare services, deepen the reform of “go once at most” on healthcare services, propel “internet + Healthcare”, optimize the transfer and connection of medical insurance relations and medical settlement of different places, promote nearest medical insurance handling services, optimize the agreement management of designated medical institutions, improve the medical insurance handling and management service system, strengthen data support of medical insurance services, create demonstration window for medical insurance handling services and crack down on insurance fraud in medical insurance sector.

Medical Practitioners

In June 1998, the SCNPC promulgated the Law on Licensed Medical Practitioners of the People’s Republic of China, or the Licensed Medical Practitioners Law, which became effective in May 1999 and was amended in 2009. According to the Licensed Medical Practitioners Law, registered doctors can work in medical or healthcare institutions according to the registered place, category and scope of business to engage in the relevant services of medical treatment, prevention or healthcare. Person who fails to register as a doctor and obtain the practicing certificate shall not practice medicine. In February 2017, the NHFPC promulgated the Administrative Measures for the Registration of Medical Practitioners, or the Medical Practitioners Registration Measures, which became effective in April 2017 and stipulate that medical practitioners shall obtain the Practice License for Medical Practitioners to practice upon registration.

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In November 2014, the NHFPC, the NDRC, the MOHRSS, the SATCM and the China Insurance Regulatory Commission jointly promulgated Several Opinions on Promoting and Standardizing Multi-Institution Practice of Medical Practitioners. According to these opinions, the clinical, dental and traditional Chinese medicine practitioners are allowed to practice in multiple places. The medical practitioners who meet certain requirements and conditions shall register with competent health administrative authorities and obtain the consent from the medical institution where he or she first practices before practicing in other places. Moreover, under the Medical Practitioners Registration Measures, a medical practitioner practicing in multiple institutions at the same place of practice shall determine one institution as his or her primary practicing institution, and apply for registration to the competent administrative authorities of health and family planning that approve the practice at such institution, and for other institutions where a medical practitioner intends to practice, he or she should apply for the record at the relevant administrative authorities of health and family planning that approve the practice of such institutions, which names should be indicated in the record. In addition, a medical practitioner intends to add the practicing institution beyond the place of practice, he or she should apply for registering such institution to the relevant administrative authorities of health and family planning authority that approve the practice of such institutions.

According to the Measures for the Administration of Prescriptions issued by the NHFPC in February 2007, a registered medical practitioner shall obtain the corresponding prescription right at the registered practice place and the registered medical practitioner shall issue prescriptions according to the relevant requirements. The prescriptions issued by a registered assistant medical practitioner shall not become effective until it is signed by a registered medical practitioner.

In August 2021, the SCNPC promulgated the Law on Medical Practitioners of the People's Republic of China, or the Medical Practitioners Law, which became effective in March 2022 and replaced the Licensed Medical Practitioners Law. According to the Medical Practitioners Law, medical practitioners who practice regularly in two or more medical and health institutions shall mainly practice in one of the institutions, and shall go through relevant procedures provided by the State. Medical practitioners may, in accordance with the relevant provisions of the State and with the consent of their medical and health institutions, provide medical and health services for some of the common diseases, chronic diseases and other appropriate diseases through the internet or other information technologies. The State supports telemedicine cooperation among medical and health institutions through the internet or other information technologies.

Regulations Relating to Food Business

General Administration on Food Operation

The Food Safety Law of the People's Republic of China, which was effective as from June 2009 and amended by the SCNPC in April 2015 , December 2018 and April 2021 and became effective in April 2021, and the Implementation Regulations of the Food Safety Law of the PRC, which took effect as from July 2009 and were amended by the State Council in 2016 and 2019, regulate food safety and set up a system of the supervision, monitoring and evaluation of food safety and adopt food safety standards. The State Council implements a licensing system for the food production and transaction. To engage in food production, sale or catering services, the business operator shall obtain a license in accordance with the laws , with an exception for sales of edible agricultural products or prepackaged food. Sales of prepackaged food shall be filed with relevant food safety administrations. Furthermore, the State Council implements strict supervision and administration for special categories of foods such as healthcare food, special formula foods for medical purposes and infant formula.

The Administrative Measures for Food Business Licensing, promulgated by the CFDA in August 2015 and amended in 2017 regulates the food business licensing activities, strengthens the supervision and management of food business and ensures food safety. Food business operators shall obtain one Food Business License for one business venue where they engage in food business activities. The valid term of a food business license is five years.

Regulations Relating to Product Quality and Consumers Protection

According to the Product Quality Law of the People's Republic of China, which was effective as from September 1993 and amended by the SCNPC in 2000, 2009 and 2018, respectively, products for sale must satisfy relevant safety standards and sellers shall adopt measures to maintain the quality of products for sale. Sellers may not sell mix impurities or imitations into products, or substitute fake products for genuine ones, or substitute defective products for good ones or substitute substandard products for standard ones. For sellers, any violation of state or industrial standards for health and safety or other requirements may result in civil liabilities and administrative penalties, such as compensation for damages, fines, confiscation of products illegally sold and the proceeds from such sales and even revoking business license; in addition, severe violations may subject the responsible individual or enterprise to criminal liabilities.

According to the Consumers Rights and Interests Protection Law of the People's Republic of China, or Consumers Rights and Interests Protection Law, which became effective in January 1994 and was amended by the SCNPC in 2009 and 2013 respectively, business operators should guarantee that the products and services they provide satisfy the requirements for personal or property safety, and provide consumers with authentic information about the quality, function, usage and term of validity of the products or services. The consumers whose interests have been damaged due to the products or services that they purchase or accept on the internet trading platforms may claim damages to sellers or service providers. Where the operators of the online trading platforms are unable to provide the real names, addresses and valid contact details of the sellers or service providers, the consumers may also claim damages to the providers of the online trading platforms. Operators of online trading platforms that clearly knew or should have known that sellers or service providers use their platforms to infringe upon the legitimate rights and interests of consumers but fail to take necessary measures must bear joint and several liabilities with the sellers or service providers. Moreover, if business operators deceive consumers or knowingly sell substandard or defective products, they should not only compensate consumers for their losses, but also pay additional damages equal to three times the price of the goods or services.

In January 2017, the SAIC issued the Interim Measures for No Reason Return of Online Purchased Products within Seven Days, which became effective in March 2017 and was amended in October 2020, further clarifying the scope of consumers' rights to make returns without a reason, including exceptions, return procedures and online trading platform operators' responsibility to formulate seven-day no-reason return rules and related consumer protection systems, continuously display such rules and systems on a notable location of the homepage, and ensure that consumers are able to read and download them conveniently and completely, and supervise the merchants for compliance with these rules.

Regulations Relating to Online Advertising

Foreign Investment on Advertising

The principal regulation governing foreign-invested advertising agencies in China are the Administrative Measures for Foreign Invested Advertising Enterprise, which was abolished due to the decision on Repealing the Administrative Measures for Foreign Invested Advertising Enterprise issued by SAIC in June 2015. According to the Negative List and the Catalog, foreign investors are allowed to own 100% of an advertising agency in China subject to certain qualification requirements. However, foreign investment in advertising agencies that provide online advertising services is still subject to restrictions of foreign investment in the value-added telecommunications business.

Administration on Internet Advertisement

In April 2015, the SCNPC enacted the Advertising Law of the People's Republic of China, or the Advertising Law, which became effective in September 2015 and was amended in October 2018 and April 2021. The Advertising Law regulates commercial advertising activities in the PRC and sets out the obligations of advertisers, advertising operators, advertising publishers and advertising spokespersons, and prohibits any advertisement from containing any obscenity, pornography, gambling, superstition, terrorism or violence-related content. Any advertiser in violation of such requirements to advertisement content will be ordered to cease publishing such advertisements and imposed a fine ranging from RMB200,000 to RMB1,000,000; in severe circumstances, the business license of such advertiser may be revoked, and the relevant authorities may revoke the approval document for advertisement examination and refuse to accept applications submitted by such advertiser for one year. In addition, any advertising operator or advertising publisher in violation of such requirements will be imposed a fine ranging from RMB200,000 to RMB1,000,000, and the advertisement fee received will be confiscated; in severe circumstances, the business license of such advertising operator or advertising publisher may be revoked.

Except that certain prescription drugs are prohibited from advertising, the advertisement of prescription drugs can be only made on designated medical or pharmaceutical journals. Any display of prescription drugs advertisements outside the designated media channels may result in violations of such restrictions by the advertising operator, confiscation of advertising fees and a fine ranging from RMB200,000 to RMB1,000,000, or, in severe circumstances, revocation of business license. In addition, any advertisement for medical treatment, pharmaceutical or medical devices must not contain any assertion or guarantee on the function and safety, or any statement on curative rate or effectiveness of such medical treatment, pharmaceutical or medical devices, and any violation of such requirements will result in a fine equivalent to an amount up to three times the amount of the advertising fees, or a fine ranging from RMB100,000 to RMB200,000 if the advertising fees cannot be calculated or are significantly low; and in severe circumstances, a fine equivalent to the amount up to five times the amount of the advertising fees will be imposed, or a fine ranging from RMB200,000 to RMB1,000,000 if the advertising fees cannot be calculated or are significantly low. Moreover, the Advertising Law also provides that the internet information service providers must not publish advertisements related to medical treatments, drugs, medical devices or health foods in the disguised form of providing healthcare and health maintenance knowledge.

The Interim Measures for Administration of Internet Advertising, or the Internet Advertising Measures regulating the internet-based advertising activities, were adopted by the SAIC in July 2016 and became effective in September 2016. According to the Internet Advertising Measures, internet advertisers are responsible for the authenticity of the advertisements content and all online advertisements must be marked "Advertisement" so that viewers can easily identify them as such. In November 2021, the SAMR released a draft of Measures for Administration of Internet Advertising, or the Draft Internet Advertising Measures, which stipulated the obligations of the advertisers, the internet advertising operators and the internet information service providers. The internet information service providers refer to the natural persons, legal persons or other organizations that provide information services through the internet but are not involved in the design, production, agency, release or other activities of internet advertising. According to the Draft Internet Advertising Measures, advertisements for medical treatment, drugs, formula foods for special medical purposes, medical devices or health food shall not be broadcast live on the internet. As of the date of this annual report, the Draft Internet Advertising Measures has yet to come into effect.

Pursuant to the Interim Administrative Measures on Drugs, Medical Devices, Health Foods and Foods for Special Medical Purposes Advertisements Examination, which took effect in March 2020, and replaced the Measures for Drug Advertisements Examination and the Measures for Medical Device Advertisement Examination, the drugs, medical devices, health foods and foods for special medical purposes advertisements shall be examined according to such measures. The applicants for such advertisements must be the holders of the registration certificate or record-filing certificate of the drugs, medical devices, health foods and foods for special medical purposes or the production or operation enterprises it authorized. The valid period of drugs, medical devices, health foods and foods for special medical purposes advertisement license numbers shall be consistent with the shortest one of the valid periods of the registration certificate, record-filing certificate or production license of the product. In the case of no valid period stipulated in such documents, the valid period of the advertisement license numbers shall be two years. And the content of approved advertisement may not be altered without prior approval, otherwise a new examination shall be reapplied for the revised content of drug and medical device advertisement.

Regulations relating to Internet Information Security and Privacy Protection

PRC government authorities have enacted laws and regulations with respect to internet information security and protection of personal information from any abuse or unauthorized disclosure. Internet information in China is regulated and restricted from a national security standpoint.

In June 2017, the Cyber Security Law of the People's Republic of China, or the Cyber Security Law, promulgated by SCNPC took effect, which is formulated to maintain the network security, safeguard the cyberspace sovereignty, national security and public interests, protect the lawful rights and interests of citizens, legal persons and other organizations, and requires that a network operator, which includes, among others, internet information services providers, take technical measures and other necessary measures to safeguard the safe and stable operation of the networks, effectively respond to the network security incidents, prevent illegal and criminal activities, and maintain the integrity, confidentiality and availability of network data. The Cyber Security Law reaffirms the basic principles and requirements set forth in other existing laws and regulations on personal information protections and strengthens the obligations and requirements of internet service providers, which include but are not limited to: (i) keeping all user information collected strictly confidential and setting up a comprehensive user information protection system; (ii) abiding by the principles of legality, rationality and necessity in the collection and use of user information and disclosure of the rules, purposes, methods and scopes of collection and use of user information; and (iii) protecting users' personal information from being leaked, tampered with, destroyed or provided to third parties. Any violation of the provisions and requirements under the Cyber Security Law and other related regulations and rules may result in administrative liabilities such as warnings, fines, confiscation of illegal gains, revocation of licenses, suspension of business, and shutting down of websites, or, in severe cases, criminal liabilities.

In addition, the PRC Data Security Law took effect in September 2021. The Data Security Law establishes a tiered system for data protection in terms of their importance. Data categorized as "important data," which will be determined by governmental authorities in the form of catalogs, are required to be treated with higher level of protection. Specifically, the Data Security Law provides that operators processing "important data" are required to appoint a "data security officer" and a "management department" to take charge of data security. In addition, such operator is required to evaluate the risks of its data activities periodically and file assessment reports with relevant regulatory authorities. Numerous regulations, guidelines and other measures have been or are expected to be adopted under the umbrella of, or in addition to, the Cyber Security Law and Data Security Law. For example, Regulations on the Security Protection of Critical Information Infrastructure, or the CII Protection Regulations, became effective in September 2021. According to the CII Protection Regulations, critical information infrastructure, or the CII, refers to any important network facilities or information systems of the important industry or field such as public communication and information service, energy, transportation, water conservancy, finance, public services, e-government affairs and national defense science, which may endanger national security, people's livelihood and public interest in the case of damage, function loss or data leakage. Regulators supervising specific industries are required to formulate detailed guidance to identifies CII in the respective sectors, and a critical information infrastructure operator, or a CIIO, must take the responsibility to protect the CII's security by performing certain prescribed obligations. For example, CIIOs are required to conduct network security test and risk assessment, report the assessment results to relevant regulatory authorities, and timely rectify the issues identified at least once a year. As of the date of this annual report, we have not been identified by a CIIO by the relevant regulatory authority.

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In September 2021, the CAC, the MIIT, and other governmental authorities issued Guidance on Strengthening the Comprehensive Governance of Internet Information Service Algorithms, which propose improving algorithm security governance mechanism and promoting algorithm filing. In December 2021, the CAC promulgated the Administrative Provisions on Internet Information Service Algorithm Recommendation, which became effective in March 2022 and implements classification and hierarchical management for algorithm recommendation service providers based on various criteria, and stipulates that algorithm recommendation service providers with public opinion attributes or social mobilization capabilities shall file with the CAC within ten business days from the date of providing such services. The MIIT published the draft of Data Security Management Measures in the Field of Industry and Information Technology (Trial) in September 2021 and February 2022, which requires the industrial and telecom data processors to further implement data classification and hierarchical management, take necessary measures to ensure that data remains effectively protected and being lawfully applied and conduct data security risk monitoring. As of the date of this annual report, the draft measures have not been formally adopted.

In July 2013, the MIIT issued the Provisions on Protecting Personal Information of Telecommunication and Internet Users to further define the personal information of user to include user name, birthday, identification number, address, phone number, account, passcode, and others that may be used to identify the user solely in addition to other information such as location and service time of users. Furthermore, according to the interpretations issued by the Supreme People's Court and the Supreme People's Procuratorate in May 2017, personal information means various information recorded electronically or through other manners, which may be used to identify individuals or activities of individuals, including but not limited to the name, identification number, contact information, address, user account and passcode, property ownership and location tracking. According to the Announcement on Launching Special Crackdown against Illegal Collection and Use of Personal Information by Apps promulgated by the CAC, the MIIT and the Ministry of Public Security of the People's Republic of China in January 2019, application operators shall strictly perform their obligations under the Cyber Security Law when collecting and using personal information, be responsible for the security of personal information obtained, and take effective measures to strengthen personal information protection. In July 2020, the MIIT issued the Notice on Carrying out Special Rectification Actions in Depth against the Infringement on Users' Rights and Interests by Apps to urge app service providers, among others, to strengthen the protection of users' personal information in relation to the download and usage of apps. In March 2021, the CAC the MIIT, the Ministry of Public Security of the PRC and the SAMR jointly issued the Provision on Scope of Necessary Personal Information for Common Types of Mobile Internet Applications to further provide guidance over personal information security and privacy protection.

In November 2015, the Ninth Amendment to the Criminal Law issued by the SCNPC became effective, pursuant to which, any internet service provider that fails to comply with obligations related to internet information security administration as required by applicable laws and refuses to rectify upon order is subject to criminal penalty for (i) any large-scale dissemination of illegal information; (ii) any severe consequences due to the leakage of the user information; (iii) any serious loss of criminal evidence; or (iv) other severe circumstances. Furthermore, any individual or entity that (i) sells or distributes personal information in a manner which violates relevant regulations, or (ii) steals or illegally obtain any personal information is subject to criminal penalty in severe circumstances.

In October 2021, the CAC published the Safety Assessment Measures for Data Outbound Transfer (Draft for Comments), which stipulate that the data processors who transfer important data and personal information that are collected and generated within the territory of the People's Republic of China outbound should be subject to security assessment. The draft measures further stipulate the process and requirements for the security assessment. In November 2021, the CAC published the Regulations of Internet Data Security Management (Draft for Comments), which further regulate the internet data processing activities and emphasize the supervision and management of network data security, and further stipulate the obligations of internet platform operators, such as establish a system for disclosure of platform rules, privacy policies and algorithmic strategies related to data, and timely disclosure of formulation procedures and adjudication procedures and more. As of the date of this annual report, these drafts have been released for public comment only and have not been formally adopted. The final provisions and the timeline for its adoption are subject to changes and uncertainties.

The Personal Information Protection Law took effect in November 2021, integrates the various rules with respect to personal information rights and privacy protection and applies to the processing of personal information within mainland China as well as certain personal information processing activities outside mainland China, including those for the provision of products and services to natural persons within China or for the analysis and assessment of acts of natural persons within China.

Furthermore, in December 2021, the CAC and several other administrations jointly promulgated the amended Cybersecurity Review Measures, or the Cybersecurity Review Measures, which took effect in February 2022. Pursuant to the Cybersecurity Review

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Measures, where the relevant activity affects or may affect national security, a CIO that purchases network products and services, or an internet platform operator that conducts data process activities, shall be subject to the cybersecurity review. The Cybersecurity Review Measures also expands the cybersecurity review requirement to cover “internet platform operators” in possession of personal information of over one million users if such operators intend to list their securities in a foreign country. Additionally, relevant governmental authorities in the PRC may initiate cybersecurity review if they determine an internet platform operator’s network products or services or data processing activities affect or may affect national security. In November 2021, Measures on Network Data Security Management (Draft for Comment), or the Draft Measures on Network Data, was proposed by the CAC for public comments until December 13, 2021. The Draft Measures on Network Data requires data processors to apply for cybersecurity review in accordance with the relevant laws and regulations for carrying out activities including but not limited to: (i) a merger, reorganization, or division to be conducted by an Internet platform operator who has amassed a substantial amount of data resources that concern national security, economic development or the public interest, which will or may impact national security; (ii) an overseas initial public offering to be conducted by a data processor processing the personal information of more than one million individuals; (iii) an overseas initial public offering in Hong Kong to be conducted by a data processor, which will or may impact national security; and (iv) other data processing activities that will or may have an impact national security. Any failure to comply with such requirements may subject us to, among others, suspension of services, fines, revoking relevant business permits or business licenses and penalties. The Draft Measures on Network Data was released for public comment only, there remains substantial uncertainty, including but not limited to its final content, adoption timeline, effective date or relevant implementation rules.

Regulations Relating to Intellectual Property

Copyright

China has adopted comprehensive legislation governing intellectual property rights, including trademarks and copyrights. China is a signatory to the primary international conventions on intellectual property rights and has been a member of the Agreement on Trade Related Aspects of Intellectual Property Rights since its accession to the WTO in December 2001.

In September 1990, the SCNPC promulgated the Copyright Law of the People’s Republic of China, effective in June 1991 and amended in 2001, 2010 and 2020 respectively and the latest amendment will take effect on June 1, 2021. The amended Copyright Law extends copyright protection to internet activities, products disseminated over the internet and software products. In addition, there is a voluntary registration system administered by the Copyright Protection Centre of China.

In order to further implement the Computer Software Protection Regulations, promulgated by the State Council in December 2001 and amended in 2011 and 2013 respectively, the National Copyright Administration issued Computer Software Copyright Registration Procedures in February 2002, which specify detailed procedures and requirements with respect to the registration of software copyrights.

Trademark

According to the Trademark Law of the People’s Republic of China, promulgated by the SCNPC in August 1982, and amended in 1993, 2001, 2013 and 2019 respectively, the Trademark Office of the SAMR is responsible for the registration and administration of trademarks in China. The SAMR under the State Council has established a Trademark Review and Adjudication Board for resolving trademark disputes. Registered trademarks are valid for ten years from the date the registration is approved. A registrant may apply to renew a registration within twelve months before the expiration date of the registration. If the registrant fails to apply in a timely manner, a grace period of six additional months may be granted. If the registrant fails to apply before the grace period expires, the registered trademark shall be deregistered. Renewed registrations are valid for ten years. In April 2014, the State Council issued the revised Implementation of the Trademark Law, which specified the requirements of applying for trademark registration and review.

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Patent

According to the Patent Law of the People's Republic of China promulgated by the SCNPC in 1984 and amended in 1992, 2000 and 2008, respectively, a patentable invention or a utility model must meet three criteria: novelty, inventiveness and practicability. A patent is valid for a twenty-year term for an invention and a ten-year term for a utility model or design, starting from the application date.

Domain Names

In May 2012 and June 2019, the China Internet Network Information Center issued the Implementing Rules for Domain Name Registration and the Implementing Rules for National Top-level Domain Name Registration setting forth the detailed rules for registration of domain names and top-level domain names. In August 2017, the MIIT promulgated the Administrative Measures on Internet Domain Names, or the Domain Name Measures. The Domain Name Measures regulate the registration of domain names, such as the top-level domain name ".cn".

Regulations Relating to Foreign Exchange and Dividend Distributions

The principal regulations governing foreign currency exchange in China are the Foreign Exchange Administration Regulations, which was promulgated by the State Council in January 1996, which became effective in April 1996 and was subsequently amended in 1997 and 2008 and the Regulations on the Administration of Foreign Exchange Settlement, Sale and Payment which was promulgated by the PBOC in June 1996 and became effective in July 1996. Under these regulations, the Renminbi for current account items is freely convertible, including the distribution of dividends, interest payments, trade and service-related foreign exchange transactions, but not for capital account items, such as direct investments, loans, and investments in securities outside of the PRC, unless the prior approval of the SAFE or its local counterpart is obtained. Foreign invested enterprises are permitted to convert their after-tax dividends into foreign exchange and to remit such foreign exchange out of their foreign exchange bank accounts in the PRC.

The principal regulations governing distribution of dividends of foreign holding companies include the Foreign Investment Enterprise Law and the Administrative Rules under the Foreign Investment Enterprise Law, which have been abolished by the Foreign Investment Law on January 1, 2020. Under current regulations, all PRC enterprises, including foreign investment enterprises, are required to allocate at least 10% of their after-tax profits to statutory reserve funds unless these reserve funds have reached 50% of the registered capital of the enterprises. These reserve funds are not distributable as cash dividends and dividends shall not be distributed until any losses from prior fiscal years have been offset. Furthermore, under the EIT Law, which became effective in January 2008 and amended in 2018, the maximum tax rate for the withholding tax imposed on dividend payments from PRC foreign invested companies to their overseas investors that are not regarded as "resident" for tax purposes is 20%. The rate was reduced to 10% under the Implementing Regulations for the EIT Law issued by the State Council. However, a lower withholding tax rate might be applied if there is a tax treaty between China and the jurisdiction of the foreign holding companies, such as tax rate of 5% in the case of Hong Kong companies that holds at least 25% of the equity interests in the foreign-invested enterprise, and certain requirements specified by PRC tax authorities are satisfied.

Regulations Relating to Stock Incentive Plans

According to the Notice of Issues Related to the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Listed Company, or the Share Incentive Rules, which was issued by the SAFE in February 2012 and other regulations, directors, supervisors, senior management and other employees participating in any share incentive plan of an overseas publicly-listed company who are PRC citizens or non-PRC citizens residing in China for a continuous period of not less than one year, subject to certain exceptions, are required to register with the SAFE. All such participants need to authorize a qualified PRC agent, such as a PRC subsidiary of overseas publicly-listed company to register with the SAFE and handle foreign exchange matters such as opening accounts, transferring and settlement of the relevant proceeds. The Share Incentive Rules further require an offshore agent to be designated to handle matters in connection with the exercise of share options and sale of proceeds for the participants of share incentive plans.

Failure to complete the SAFE registrations for our employee incentive plans after our listing may subject them to fines and legal sanctions, and may also limit our ability to contribute additional capital into our PRC subsidiaries and limit our PRC subsidiaries' ability to distribute dividends to us.

Regulations Relating to Employment

The Labor Law of the People's Republic of China, or the Labor Law, which became effective in January 1995 and was amended in 2009 and 2018, and the Employment Contract Law of the People's Republic of China, or the Employment Contract Law, effective in January 2008 and amended in 2012, require employers to provide written contracts to their employees, restrict the use of temporary workers and aim to give employees long-term job security. Employers must pay their employees wages equal to or above local minimum wage standards, establish labor safety and workplace sanitation systems, comply with state labor rules and standards and provide employees with appropriate training on workplace safety. In September 2008, the State Council promulgated the Implementing Regulations for the PRC Employment Contract Law which became effective immediately and interprets and supplements the provisions of the Employment Contract Law.

Under the Labor Contract Law, an employer shall limit the number of dispatched workers so that they do not exceed a certain percentage of its total number of workers. In January 2014, the MOHRSS issued the Interim Provisions on Labor Dispatching, which became effective in March 2014, pursuant to which it provides that the number of dispatched workers used by an employer shall not exceed 10% of the total number of its employees.

The PRC governmental authorities have passed a variety of laws and regulations regarding social insurance and housing funds from time to time, including, among others, the Social Insurance Law of the People's Republic of China, the Regulation of Insurance for Labor Injury, the Regulations of Insurance for Unemployment, the Provisional Insurance Measures for Maternal Employees and the Administrative Regulations on the Housing Provident Fund. Pursuant to these laws and regulations, PRC companies must make contributions at specified levels for their employees to the relevant local social insurance and housing fund authorities. Failure to comply with such laws and regulations may result in various fines and legal sanctions and supplemental contributions to the local social insurance and housing fund regulatory authorities.

Regulation Relating to Taxation

Enterprise Income Tax

Pursuant to the EIT Law promulgated by the National People's Congress on March 16, 2007, which became effective from January 1, 2008 and was amended in 2017 and 2018, the income tax rate for both domestic and foreign-invested enterprises incorporated in the PRC is 25% commencing from January 1, 2008. In order to clarify certain provisions in the EIT Law, the State Council promulgated the Implementation Rules of the Enterprise Income Tax Law of the PRC, or the EIT Implementation Rules, on December 6, 2007, which became effective on January 1, 2008 and was amended in 2019. Under the EIT Law and the EIT Implementation Rules, enterprises are classified as either "resident enterprises" or "non-resident enterprises". Pursuant to the EIT Law and the EIT Implementation Rules, besides enterprises established within the PRC, enterprises established outside of the PRC whose "de facto management bodies" are located in the PRC are considered as "resident enterprises" and subject to the uniform enterprise income tax rate of 25% for their global income. In addition, the EIT Law provides that a non-resident enterprise refers to an entity established under foreign law whose "de facto management bodies" are not within the PRC but which have an establishment or place of business in the PRC, or which do not have an establishment or place of business in the PRC but have income sourced within the PRC.

Enterprises that are recognized as high and new technology enterprises in accordance with the Administrative Measures Recognition of High and New Technology Enterprises are entitled to enjoy the preferential enterprise income tax rate of 15%. The validity period of the high and new technology enterprise qualification shall be three years from the date of issuance of the certificate of high and new technology enterprise. The enterprise can re-apply for such recognition as a high and new technology enterprise before or after the previous certificate expires. The enterprise shall, after being recognized as a high and new technology enterprise, fill out and submit annually the statements on annual development conditions for the previous year. Besides, if a high and new technology enterprise has changed its name or has undergone any major change concerning the recognition conditions (such as a division, merger, reorganization or change of business), it shall report the change within three months and recognition institution will review whether it continues to be qualified as high and new technology enterprise. 1 Pharmacy Technology has obtained the certificate of high and new technology enterprise on December 6, 2019.

Dividend Withholding Tax

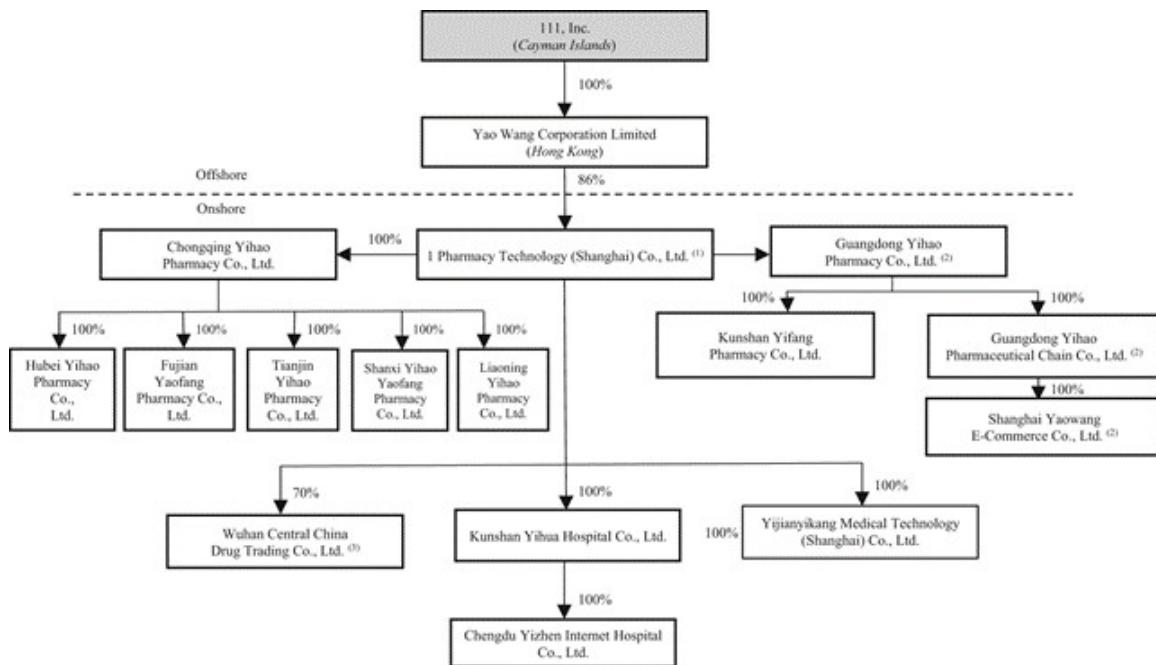
The EIT Implementation Rules provide that, from January 1, 2008, an income tax rate of 10% will normally be applicable to dividends declared to non-PRC resident enterprise shareholders that do not have an establishment or place of business in the PRC, or that have such establishment or place of business but whose relevant income is not effectively connected with the establishment or place of business, to the extent such dividends are derived from sources within the PRC. The income tax on dividends may be further reduced pursuant to a tax treaty between the PRC and the jurisdictions in which non-PRC shareholders reside.

Value-Added Tax

Pursuant to the Provisional Regulation of the PRC on Value-Added Tax, which was promulgated by the State Council on December 13, 1993 and amended in 2008, 2016 and 2017 and its implementation rules, entities or individuals engaging in the sale of goods, the provision of processing services, repairs and replacement services, sale of services, intangible assets or real property, or the importation of goods within the territory of the PRC must pay value-added tax.

C. Organizational Structure

The following diagram illustrates our corporate structure, including our principal subsidiaries, consolidated affiliated entities and subsidiaries of consolidated affiliated entities as of the date of this annual report on Form 20-F:



- (1) The shareholders of 1 Pharmacy Technology include Yao Wang Corporation Limited (86%) and various investors (14%) who purchased shares in 1 Pharmacy in connection with capital injection. See “Item 4. Information on the Company —A. History and Development of the Company.”
- (2) Guangdong Yihao Pharmacy Co., Ltd., Guangdong Yihao Pharmaceutical Chain Co., Ltd. and Shanghai Yaowang E-Commerce Co., Ltd. were our VIEs prior to the termination of the contractual arrangements and transfer of equity interests in February 2022, at which time these entities became our directly owned subsidiaries.
- (3) The shareholders of Wuhan Central China Drug Trading Co., Ltd. include 1 Pharmacy Technology (70%) and Wuhan Zall Venture Capital Co., Ltd. (30%).

D. Property, Plant and Equipment

As of December 31, 2021, we leased office space in Shanghai with an area of approximately 5,589.3 square meters. As of December 31, 2021, we also leased office space in Beijing, Chengdu, Chongqing, Tianjin, Hefei, Fuzhou, Xi'an, Guangzhou and Shenyang with a total area of approximately 4,889.3 square meters. In addition, we leased properties in various locations in China for operations of Yi Hao Pharmacies, with a total area of approximately 2,953.7 square meters as of December 31, 2021. With respect to our fulfillment centers, we leased these facilities with a total area of approximately 228,934 square meters in Kunshan, Tianjin, Chongqing, Wuhan, Fuzhou, Xi'an, Shenyang and Zhaoqing as of December 31, 2021. We lease our premises from unrelated third parties under operating lease agreements.

Item 4A. Unresolved Staff Comments

None.

Item 5. Operating and Financial Review and Prospects

The following discussion of our financial condition and results of operations is based upon, and should be read in conjunction with, our audited consolidated financial statements and the related notes included in this annual report on Form 20-F. This report contains forward-looking statements. See "Forward-Looking Information." In evaluating our business, you should carefully consider the information provided under the caption "Item 3. Key Information—D. Risk Factors" in this annual report on Form 20-F. We caution you that our businesses and financial performance are subject to substantial risks and uncertainties.

A. Operating Results

Overview

We are dedicated to digitally connecting patients with drugs and healthcare services in China. We are a leading integrated online and offline healthcare platform with the largest virtual pharmacy network in China. By applying advanced Internet and enabling technology, we deliver a broad range of products and services ranging from medical consultations to prescription drugs, from health and wellness products to tools from one-time fix to life-cycle chronic disease management, from off-line to online, as well as support services that help them better manage their conditions, through optimized supply chain and cloud services, to increase the efficiency and transparency of drug retail and distribution. Today, we provide hundreds of millions of consumers with better access to pharmaceutical products and medical services, bridging medical providers and patients. Our integrated business model is hallmark by our flagship technology platforms:

- **1 Medicine Marketplace:** Our virtual retail pharmacy provides consumers with a wide variety of pharmaceutical products and other merchandise.
- **1 Clinic:** Our internet hospital provides consumers with cost-effective and convenient online consultation and electronic prescription services.
- **1 Pharmacy:** Our online wholesale pharmacy serves as a one-stop shop for pharmacies to source a vast selection of pharmaceutical products.

We are building our core competencies in the areas of smart supply chain, cloud-based solutions, big data and medical expertise, and are reshaping the pharmaceutical value chain in China using our New Retail platform. Not only do we serve consumers directly through our online retail pharmacy, we also enable more than 13 offline pharmacies to better serve their consumers as of December 31, 2021. Our online wholesale pharmacy, 1 Pharmacy, serves as a one-stop shop for pharmacies to source a vast selection of pharmaceutical products.

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We connect pharmacies, pharmaceutical companies, medical professionals and consumers in our ecosystem, and we improve the efficiency and transparency of the pharmaceutical value chain. Our omni-channel e-commerce platform plays an important role in facilitating the commercialization of drugs across the nation. This model offers multiple channels for pharmaceutical companies to simultaneously reach healthcare providers nationwide and educates them about new drugs and therapies. This model significantly reduces time, resources and cost, which allows drugs to be distributed quickly and efficiently.

Our revenue was RMB3.95 billion in 2019, RMB8.20 billion in 2020 and RMB12.43 billion (US\$1.95 billion) in 2021, of which product revenues from the B2B segment were RMB3.29 billion, RMB7.49 billion and RMB11.84 billion (US\$1.86 billion), respectively. Our net loss as a percentage of net revenues decreased from 12.7% in 2019 to 5.7% in 2020 and further to 5.0% in 2021.

Key Factors Affecting Our Results of Operations

Our results of operations are affected by general factors driving China's general health and wellness industry, especially pharmaceutical retail and wholesale distribution and internet healthcare industries in China.

Our business expansion and revenue growth have been and will continue to be affected by the development of the general health and wellness industry in China, which is in turn driven by increasing disposable income and healthcare spending, rising awareness of health, an aging population, increasing life expectancy, increasing penetration of mobile internet, favorable government policies and increasing coverage of medical insurance. Unfavorable changes in any of these general industry conditions could negatively affect demand for our products and services and negatively and materially affect our results of operations.

We are affected by government policies and regulations that address all aspects of our operations, including qualifications and licensing requirements for online and offline sales and distribution of pharmaceutical and other health and wellness products, online healthcare services and online hospitals, among other things. See also "Item 3. Key Information—D. Risk Factors—Risks Related to Our Business and Industry—We are subject to extensive and evolving regulatory requirements, non-compliance with which, or changes in which, may materially and adversely affect our business and prospects." We have benefitted from certain recent favorable regulatory and policy changes in China, especially various policy initiatives that have promoted the distribution of pharmaceutical products. We expect that the implementation of these measures relating to the distribution of pharmaceutical products will also affect market competition and drive industry consolidation.

While our business is influenced by general factors driving the general health and wellness market in China, we believe our results of operations are more directly affected by company-specific factors, including the following major factors.

Our Ability to Attract and Retain Consumers and Pharmacies

Our net revenues are dependent on our ability to attract and retain our consumers and pharmacies.

- *Consumers* . Historically, our revenue growth was primarily driven by the sale of pharmaceutical and other health and wellness products through our online retail pharmacy to consumers. Steady and continued growth of our consumer base and their stickiness to our platform allows us to maintain a solid foundation for our business to continue to expand.
- *Pharmacies* . Since we launched our online wholesale pharmacy, 1 Pharmacy, in May 2017, we have significantly increased the scale of our B2B business through the sale of pharmaceutical products to pharmacies. As of December 31, 2021, we have served more than 385,000 pharmacies, compared to over 329,000 pharmacies as of December 31, 2020 and 235,000 pharmacies as of December 31, 2019. We have also diversified the types of pharmacy customers we serve and have expanded our reach not only to independent pharmacies and pharmacy chains, but also to in-house pharmacies within clinics and private hospitals. We have thus far accumulated considerable offline pharmacy resources, which contributed to the increase of product revenues from the B2B segment to RMB11.84 billion (US\$1.86 billion) in 2021. We expect to further expand our offline pharmacy market and to develop this revenue stream. Product revenues from the B2B segment contributed 83.3%, 91.3% and 95.3% to our total net revenues in 2019, 2020 and 2021, respectively.

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We rely on a diverse array of online marketing channels to attract consumers, including using social media such as WeChat and Weibo and paid placement on major online search engines in China. With respect to growing our pharmacy customers, we rely on the effective operation of our on-the-ground sales force to promote our products and services. Our ability to continue to reach more consumers and pharmacies will affect the growth of our business and our net revenues.

Our Ability to Create Value for Participants in the Healthcare Ecosystem and Increase Monetization

We are a pioneer in developing and applying technologies to create an integrated online and offline platform in the healthcare ecosystem in China. Our results of operations depend on our ability to create value for various participants in the healthcare ecosystem and increase monetization for these participants. Consumers and pharmacies are drawn to our platform because we offer a wide selection of competitively priced pharmaceutical and other health and wellness products, as well as efficient and comprehensive services. In addition, we offer to suppliers, pharmaceutical companies, medical professionals and other participants in the ecosystem our innovative cloud-based solutions, such as data service, CSO, smart supply chain services and other value-added services. Our success depends on our ability to continuously offer attractive products and services, therefore increasing user stickiness and attracting more participants to our close-loop online and offline platform. We have also implemented various initiatives and invested significantly to ramp up our cloud-based solutions and improve our smart supply chain services. As we further enhance our technologies and IT infrastructure, we aim to create more value for these participants, increasing their engagement and connection and deepening our penetration in the healthcare ecosystem, which we anticipate will create additional monetization venues for us to drive our revenue growth.

Our Ability to Manage Our Mix of Product and Service Offerings

Our results of operations are also affected by the mix of products and services we offer. We currently derive our revenues primarily from the sale and distribution of pharmaceutical and other health and wellness products to our pharmacy customers and consumers. We also earn commissions and service fees from marketplace sellers on our online marketplace. Different products and services have different cost structures. For example, the various services we provide generally have higher fixed costs. The revenue contributions from our online direct sales model, our online marketplace model and our services have a major influence on our profitability. We intend to better manage the mix of our product and service offerings in order to improve our profitability.

Our Ability to Control Operating Costs and Expenses and Improve Efficiency

Our cost of products sold represents primarily the purchase price of products and inbound shipping charges if any, as well as inventory write-downs. As our business further grows in scale, we expect to obtain more favorable terms from suppliers, including pricing terms, credit period and volume-based rebates. In addition, we aim to create value for our suppliers, especially pharmaceutical companies, by providing an effective and transparent channel for selling large volumes of their products online and by offering them valuable data insights on market demand, customer preferences and supply chain information. We believe this value proposition will also help us deepen our relationships with suppliers, obtain favorable terms and reduce our procurement costs. Our selling and marketing expenses are a significant contributor to our operating costs and expenses, and they primarily consist of payroll, bonus and employee benefits of sales and marketing staff, advertising costs, agency fees and costs for promotional materials. In 2019, 2020 and 2021, selling and marketing expenses amounted to 8.6%, 4.9% and 4.1% of our total net revenues, respectively. We expect our selling and marketing expenses to remain substantial in absolute terms as we implement new business initiatives, such as deploying additional sales personnel to promote our 1 Pharmacy and our value-added services to pharmacies. As our business grows, we anticipate that our technology and fulfillment expenses will increase in absolute terms in the foreseeable future in light of our anticipated expansion and investment plans.

We continuously seek to streamline our operations and improve our supply chain and inventory management. Controlling costs and operating expenses to achieve optimal operating efficiency is important to our success. As our business grows in scale, we expect to have significant operating leverage and realize structural cost savings.

Key Components of Results of Operations

Net Revenues

The following table sets forth the components of our net revenues by amounts and percentages of our total net revenues for the periods presented:

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	For the Year Ended December 31,							
	2019		2020		2021			
	RMB	%	RMB	%	RMB	US\$	%	
Product revenues								
B2C	636,430	16.1	666,223	8.1	491,855	77,182	3.9	
B2B	3,293,268	83.3	7,490,449	91.3	11,839,850	1,857,931	95.3	
Sub total	3,929,698	99.4	8,156,672	99.4	12,331,705	1,935,113	99.2	
Service revenues	22,355	0.6	46,485	0.6	94,197	14,782	0.8	
Total	3,952,053	100.0	8,203,157	100.0	12,425,902	1,949,895	100.0	

Product revenues. We historically reported our product revenues under our direct sales model from two reportable segments: the B2C segment and the B2B segment. Product revenues from our B2C segment are generated from the sale of pharmaceutical and other health and wellness products through 1 Medicine Marketplace, mobile apps, other online channels and offline pharmacies to consumers and certain enterprise customers. We also generate product revenues from the B2B segment through the sale of pharmaceutical products to pharmacies on 1 Pharmacy.

Our product revenues, in particular, those from B2B segment, have grown significantly and we expect continued growth as we attract more pharmacies as customers. Our product revenue from the B2B business segment in 2021 reached RMB11.84 billion (US\$1.86 billion), representing a 58.1% increase from 2020, and our product revenue from the B2C business segment in 2021 reached RMB491.9 million (US\$77.2 million), representing a 26.2% decrease from 2020.

Service revenues. Service revenues primarily consist of marketplace (MP) service fees we charge to marketplace sellers to which we provide access to 1 Medicine Marketplace where they are able to effectively sell their products. We charge marketplace sellers commission fees equal to an agreed percentage of the sales price of the product when a sale is completed and also charge marketplace sellers an annual non-refundable up-front fee for platform usage. We refer to these fees as MP service revenue. Since we launched our MP service, it has made substantial contribution to our service revenues. Our service revenues increased significantly by 102.6% from RMB46.5 million in 2020 to RMB94.2 million (US\$14.8 million) in 2021, which was primarily attributable to an increase of RMB21.8 million (US\$5.9 million) in B2B MP service revenues. We also generate service revenues by providing other ancillary services, mainly online medical consultation services for patients and digital marketing services for pharmaceutical companies. We expect our service revenues, although not a material contribution to our net revenues currently or in the near future, to grow as we expand our online marketplace and increase the service coverage of our cloud-based solutions, such cloud prescription services and data services to more pharmacies and pharmaceutical companies.

Operating costs and expenses

The following table sets forth the components of our operating costs and expenses by amounts and percentages of total operating costs and expenses for the periods presented:

	For the Year Ended December 31,							
	2019		2020		2021			
	RMB	%	RMB	%	RMB	US\$	%	
Operating costs and expenses:								
Cost of products sold	(3,786,870)	85.2	(7,837,325)	90.3	(11,804,807)	(1,852,432)	90.3	
Fulfillment expenses	(128,996)	2.9	(226,930)	2.6	(355,836)	(55,838)	2.7	
Selling and marketing expenses	(340,562)	7.6	(399,610)	4.6	(513,146)	(80,524)	3.9	
General and administrative expenses	(123,501)	2.8	(128,226)	1.5	(206,981)	(32,480)	1.6	
Technology expenses	(61,902)	1.4	(92,080)	1.1	(189,284)	(29,703)	1.4	
Other operating (expenses) income, net	(3,735)	0.1	7,703	(0.1)	2,012	316	0.1	
Total	<u>(4,445,566)</u>	<u>100.0</u>	<u>(8,676,468)</u>	<u>100.0</u>	<u>(13,068,042)</u>	<u>(2,050,661)</u>	<u>100.0</u>	

Cost of products sold. Cost of products sold consists of the purchase price of products and inbound shipping charges, as well as inventory write-downs, less rebates earned from vendors in the form of credits that we can apply against trade amounts owed to these vendors pursuant to binding arrangements when we complete a specified cumulative level of purchases within a specified time period. Cost of products does not include other direct costs related to costs of product sales such as shipping and handling expense, payroll

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and employee benefits for logistic staff, logistic centers rental expenses and depreciation expenses. Therefore, our cost of products sold may not be comparable to that of other companies, which include such expenses in their costs of products sold. We expect our cost of products sold to grow in absolute terms as our business continues to grow.

Fulfillment expenses. Fulfillment expenses primarily consist of payroll, bonus and employee benefits for logistics staff, logistics centers rental expenses, shipping and handling expenses and packaging expenses. We expect our fulfillment expenses as a percentage of our total net revenues to decrease because larger B2B orders reduce our cost as a percentage as a result of the way pricing is undertaken by the logistics business. In addition, we have implemented more cost-saving initiatives and continue to expand our fulfillment network to leverage our scale.

Selling and marketing expenses. Selling and marketing expenses primarily consist of payroll, bonus and employee benefits for sales and marketing staff, advertising costs, agency fees and costs for promotional materials. We expect our selling and marketing expenses to remain substantial in absolute terms as we implement new business initiatives, such as deploying additional sales personnel to promote our 1 Pharmacy and our value-added services to pharmacies.

General and administrative expenses. General and administrative expenses primarily consist of payroll, bonus and employee benefit costs for corporate employees, legal, finance, rental expenses, and other corporate overhead costs. We expect our general and administrative expenses to increase in absolute terms in the foreseeable future due to the anticipated growth of our business as well as accounting, insurance, investor relations and other public company costs, but to decrease as a percentage of our total net revenues as we leverage the scale of our business.

Technology expenses. Technology expenses primarily consist of technology infrastructure expenses, payroll, bonus and benefits of the employees, and costs associated with the computer, storage and telecommunications infrastructure for use in technology department. We expect our technology expenses to grow in absolute terms as we expand our technology team, enhance our big data analytics capabilities and develop new features and applications to better serve various participants in the healthcare ecosystem, but to decrease as a percentage of our total net revenues as we are able to leverage the scale of our business as we continue to grow.

Results of Operations

The following table sets forth a summary of our consolidated results of operations for the periods indicated. The period-to-period comparisons of results of operations should not be relied upon as indicative of future performance. This information should be read together with our audited consolidated financial statements and related notes included elsewhere in this annual report.

	For the Year Ended December 31,					
	2019		2020		2021	
	RMB	%	RMB	%	RMB	US\$
Net Revenues:						
Product revenues	3,929,698	99.4	8,156,672	99.4	12,331,705	1,935,113
Service revenues	22,355	0.6	46,485	0.6	94,197	14,782
Total net revenues	3,952,053	100.0	8,203,157	100.0	12,425,902	1,949,895
Operating costs and expenses:						
Cost of products sold	(3,786,870)	(95.8)	(7,837,325)	(95.5)	(11,804,807)	(1,852,432)
Fulfillment expenses	(128,996)	(3.3)	(226,930)	(2.8)	(355,836)	(55,838)
Selling and marketing expenses(1)	(340,562)	(8.6)	(399,610)	(4.9)	(513,146)	(80,524)
General and administrative expenses(1)	(123,501)	(3.1)	(128,226)	(1.6)	(206,981)	(32,480)
Technology expenses(1)	(61,902)	(1.6)	(92,080)	(1.1)	(189,284)	(29,703)
Other operating (expenses) income, net	(3,735)	(0.1)	7,703	0.1	2,012	316
Total operating costs and expenses	(4,445,566)	(112.5)	(8,676,468)	(105.8)	(13,068,042)	(2,050,661)
Loss from operations	(493,513)	(12.5)	(473,311)	(5.8)	(642,140)	(100,766)
Interest income	4,802	0.1	6,312	0.1	9,776	1,534
Interest expense	(3,622)	(0.1)	(8,817)	(0.1)	(5,488)	(861)
Foreign exchange (loss) gain	(10,328)	(0.2)	5,547	0.1	1,937	304
Other income, net	834	—	3,161	—	14,890	2,337
Loss before income taxes	(501,827)	(12.7)	(467,108)	(5.7)	(621,025)	(97,452)
Income tax expense	—	—	—	—	—	—
Net loss	(501,827)	(12.7)	(467,108)	(5.7)	(621,025)	(97,452)

(1) Share-based compensation expenses are allocated to operating expense line items as follows:

	For the Year Ended December 31,			
	2019		2020	
	RMB	RMB	RMB	US\$
(in thousands)				
General and administrative expenses	25,412	22,727	69,718	10,940
Selling and marketing expenses	24,772	40,562	50,532	7,930
Technology expenses	4,097	12,406	25,343	3,977
Total	54,281	75,695	145,593	22,847

The Year Ended December 31, 2021 Compared to the Year Ended December 31, 2020

Net Revenues

Our net revenues increased by 51.5% from RMB8.20 billion in 2020 to RMB12.43 billion (US\$1.95 billion) in 2021. This increase was primarily due to the significant increase in product revenues from B2B segment. Our net revenues experienced consistent monthly growth and are significantly impacted by the annual and mid-year e-commerce festivals.

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Product Revenues by Segment. Product revenues increased by 51.2% from RMB8.16 billion in 2020 to RMB12.33 billion (US\$1.94 billion) in 2021, due to an increase in the number of offline customers through which more products were sold. We experienced a significant increase in product revenues from B2B segment, which increased by 58.1% to RMB11.84 billion (US\$1.86 billion) from RMB7.49 billion last year. Product revenues from B2C segment decreased by 26.2% to RMB491.9 million (US\$77.2 million) from RMB666.2 million last year mainly attributable to a shift of resources to our B2B segment.

Service revenues. Our service revenues increased by 102.6% from RMB46.5 million in 2020 to RMB94.2 million (US\$14.8 million) in 2021, which was primarily attributable to the increase of our B2B service revenues in 2021.

Segment Cost of Products Sold

Cost of products sold increased by 50.6% from RMB7,837.3 million in 2020 to RMB11,804.8 million (US\$1,852.4 million) in 2021, in line with our overall revenue growth, which is primarily attributable to the growth of sales in the B2B segment.

Segment Profit/Loss

As a result of the foregoing, our segment profit from our B2C segment decreased by 21.4% from RMB139.3 million in 2020 to RMB109.4 million (US\$17.2 million) in 2021 because of the decrease in our revenues from the B2C segment. Our segment profit from our B2B segment increased by 125.8% from RMB226.6 million in 2020 to RMB511.7 million (US\$80.3 million) in 2021 mainly due to the optimization of our product mix, and such increase is also in line with the increase in our revenues from the B2B segment.

Operating Costs and Expenses

Our operating costs and expenses increased by 50.6% from RMB8.68 billion in 2020 to RMB13.07 billion (US\$2.05 billion) in 2021, with increases in the following categories of operating expenses.

Cost of Products Sold. Our cost of products sold increased by 50.6% from RMB7.84 billion in 2020 to RMB11.80 billion (US\$1.85 billion) in 2021, primarily due to our rapid revenue growth in B2B business.

Fulfillment Expenses. Our fulfillment expenses increased by 56.8% from RMB226.9 million in 2020 to RMB355.8 million (US\$55.8 million) in 2021, primarily as a result of the growth in our B2B business and the increased investment on expanding our warehouse facilities. Fulfillment expenses accounted for 2.9% of net revenue in 2021 as compared to 2.8% last year.

Selling and Marketing Expenses. Our selling and marketing expenses increased by 28.4% from RMB399.6 million in 2020 to RMB513.1 million (US\$80.5 million) in 2021. The increase was primarily attributable to an increase in the number of sales staffs and expenses associated with the expansion of the B2B business. Selling and marketing expenses accounted for 4.1% of net revenue in 2021 as compared to 4.9% last year.

General and Administrative Expenses. Our general and administrative expenses increased by 61.4% from RMB128.2 million in 2020 to RMB207.0 million (US\$32.5 million) in 2021. The increase was primarily due to increases in managerial staff and professional service fees. General and administrative expenses accounted for 1.7% of net revenue in 2021 as compared to 1.6% last year.

Technology Expenses. Our technology expenses increased by 105.6% from RMB92.1 million in 2020 to RMB189.3 million (US\$29.7 million) in 2021, mainly due to our increased investments in technology solutions and infrastructure. Technology expenses accounted for 1.5% of net revenue in 2021 as compared to 1.1% last year.

Net Loss

As a result of the foregoing, we recorded a net loss of RMB621.0 million (US\$97.5 million) in 2021 as compared to a net loss of RMB467.1 million in 2020.

The Year Ended December 31, 2020 Compared to the Year Ended December 31, 2019

Net Revenues

Our net revenues increased by 107.6% from RMB3.95 billion in 2019 to RMB8.20 billion in 2020. This increase was primarily due to the significant increase in product revenues from B2B segment. Our net revenues experienced consistent monthly growth and are significantly impacted by the annual and mid-year e-commerce festivals.

Product Revenues by Segment. Product revenues increased by 107.6% from RMB3.93 billion in 2019 to RMB8.16 billion in 2020, due to an increase in the number of offline pharmacies through which more products were sold. We experienced a significant increase in product revenues from B2B segment, which increased by 127.7% to RMB7.49 billion in 2020 from RMB3.29 billion in 2019. Product revenues from B2C segment increased by 4.7% to RMB666.2 million in 2020 from RMB636.4 million in 2019.

Service revenues. Our service revenues increased by 107.6% from RMB22.4 million in 2019 to RMB46.5 million in 2020, which was primarily attributable to the expansion of our B2B MP service in 2020.

Segment Cost of Products Sold

Cost of products sold increased by 107.0% from RMB3,786.9 million in 2019 to RMB7,837.3 million in 2020, in line with our overall revenue growth, which is primarily attributable to growth in sales and a change in revenue mix with a much higher proportion of B2B business.

Segment Profit/Loss

As a result of the foregoing, our segment profit from our B2C segment increased by 17.4% from RMB118.7 million in 2019 to RMB139.3 million in 2020, while our segment profit from our B2B segment increased by 387.1% from RMB46.5 million in 2019 to RMB226.6 million in 2020.

Operating Costs and Expenses

Our operating costs and expenses increased by 95.1% from RMB4.45 billion in 2019 to RMB8.68 billion in 2020, with increases in the following categories of operating expenses.

Cost of Products Sold. Our cost of products sold increased by 106.9% from RMB3.79 billion in 2019 to RMB7.84 billion in 2020, primarily due to growth in sales and a change in revenue mix with a much higher proportion of B2B business.

Fulfillment Expenses. Our fulfillment expenses increased by 75.9% from RMB129.0 million in 2019 to RMB226.9 million in 2020, primarily as a result of the growth in B2B business and the increased investment on expanding our warehouse facilities. Fulfillment expenses accounted for 2.8% of net revenue in 2020 as compared to 3.3% in 2019.

Selling and Marketing Expenses. Our selling and marketing expenses increased by 17.3% from RMB340.6 million in 2019 to RMB399.6 million in 2020. The increase was primarily attributable to increase in sales staff and expenses associated with the expansion of B2B business. Selling and marketing expenses accounted for 4.9% of net revenue in 2020 as compared to 8.6% in 2019.

General and Administrative Expenses. Our general and administrative expenses increased by 3.8% from RMB123.5 million in 2019 to RMB128.2 million in 2020. The increase was primarily due to increases in managerial staff and professional service fees. General and administrative expenses accounted for 1.6% of net revenue in 2020 as compared to 3.1% in 2019.

Technology Expenses. Our technology expenses increased by 48.8% from RMB61.9 million in 2019 to RMB92.1 million in 2020, mainly due to increase in our technology staff and expenses associated with expansion of our business. Technology expenses accounted for 1.1% of net revenue in 2020 as compared to 1.6% in 2019.

Net Loss

As a result of the foregoing, we recorded a net loss of RMB467.1 million in 2020 and a net loss of RMB501.8 million in 2019.

Taxation

Cayman Islands

We are incorporated in the Cayman Islands. The Cayman Islands currently has no income, corporation or capital gains tax and no estate duty, inheritance tax or gift tax. The Cayman Islands does not impose a withholding tax on payments of dividends to shareholders.

Hong Kong

Our subsidiary incorporated in Hong Kong is subject to Hong Kong profit tax at a rate of 16.5%. No Hong Kong profit tax has been levied as we did not have assessable profit that was earned in or derived from the Hong Kong subsidiary during the periods presented. Hong Kong does not impose a withholding tax on dividends.

China

Enterprise Income Tax. According to the EIT Law, which was promulgated on March 16, 2007 and amended in 2017 and 2018, and its implementing regulation, an income tax rate of 25% generally applies to all enterprises incorporated in the PRC, including our PRC subsidiaries. Under the EIT Law, an enterprise established outside the PRC with “de facto management bodies” within the PRC is considered a resident enterprise for PRC enterprise income tax purposes and is generally subject to a uniform 25% enterprise income tax rate on its worldwide income. Although we do not believe that 111, Inc. or Yao Wang Corporation Limited should be considered as a PRC resident enterprise for PRC tax purposes, PRC income tax at a rate of 25% would generally be applicable to our worldwide income if we were to be considered a PRC resident enterprise.

Dividend Withholding Tax. According to the EIT Law and its implementation rules, the profits of a foreign-invested enterprise arising in 2008 and thereafter that are distributed to its immediate holding company outside the PRC are subject to withholding tax at a rate of 10%, but a lower withholding tax rate will be applied if there is a beneficial tax treaty between the PRC and the jurisdiction of the foreign holding company. A holding company in Hong Kong, for example, will be eligible, with approval of the PRC local tax authority, to be subject to a 5% withholding tax rate under the Double Taxation Arrangement, if such holding company is considered to be a non-PRC resident enterprise and holds at least 25% of the equity interests in the PRC foreign-invested enterprise distributing the dividends. However, the PRC tax authorities will review preferential tax treatment under the “substance over form” principle and grant such treatment on a case-by-case basis. Therefore, if such Hong Kong holding company is not considered to be the beneficial owner of such dividends under applicable PRC tax regulations, such dividend will remain subject to withholding tax at a rate of 10%.

Value-Added Tax. According to the Provisional Regulations of the PRC on Value-added Tax promulgated by the State council on December 13, 1993 and amended in 2008, 2016 and 2017, and the Detailed Rules for the Implementation of the Provisional Regulations of the PRC on Value-added Tax which was promulgated by the MOF, and the STA on December 18, 2008 and became effective on January 1, 2009 and amended on October 28, 2011, all enterprises and individuals that engage in the sale of goods and services, the provision of tangible personal property leasing services or importation of goods shall pay value-added tax at different tax rates of 0%, 6%, 11% or 17% due to different business; in addition, the small-scale taxpayers shall be subject to tax rate of 3%, except as otherwise specified by the State Council. On April 4, 2018, the MOF and the STA issued the Notice on Adjusting Value-added Tax Rate, which became effective from May 1, 2018 and stipulates that the previous tax rate of 17%, 11% for the taxable sale activities or importing goods will be adjusted to 16% and 10% respectively. Moreover, on the same date, the MOF and the STA issued another notice to unify the criteria of small-scale value-added tax payers, which became effective from May 1, 2018. On March 20 2019, the MOF and the STA further issued the Notice on Adjusting Value-added Tax Rate, which became effective from April 1, 2019 and stipulates that the previous tax rate of 16%, 10% for the taxable sale activities or importing goods will be adjusted to 13% and 9% respectively. On November 16, 2011, the MOF and the STA promulgated a Pilot Plan for Imposition of Value-Added Tax to Replace Business Tax in Shanghai, or Pilot Plan, which became effective on January 1, 2012 and stipulates that any entity in Shanghai that falls in the category of “selected modern service industries” was required to switch from being a business tax payer to become a value-added tax payer, who is permitted to offset expenses incurred in providing the relevant services it provides from the taxable income. The Pilot Plan was expanded to other regions in September 2012, and was further expanded nationwide beginning on August 1, 2013. The MOF and the STA subsequently promulgated several circulars in December 2013, April 2014 and March 2016 to further expand the scope of services which are to be subject to value-added tax instead of business tax.

Inflation

To date, inflation in China has not materially affected our results of operations. According to the National Bureau of Statistics of China, the year-over-year percent changes in the consumer price index for December 2019, 2020 and 2021 were increases of 4.5%, 0.2% and 1.5%, respectively. Although we have not been materially affected by inflation in the past, we may be affected if China experiences higher rates of inflation in the future.

B. Liquidity and Capital Resources

To date, we have financed our operations primarily through cash generated by the issuance of preferred shares in private placements and our initial public offering in 2018. As of December 31, 2019, 2020 and 2021, we had RMB581.3 million, RMB1.19 billion and RMB661.4 million (US\$103.8 million), respectively, in cash and cash equivalents. Our cash and cash equivalents primarily consist of cash on hand and demand deposits.

In addition, as of December 31, 2019, 2020 and 2021, we had nil, RMB300.2 million and RMB182.6 million (US\$28.6 million), respectively, in short-term investments. Our short-term investments consist of structured deposits from commercial banks with guaranteed principal and variable interest rates indexed to the performance of underlying assets and fund products purchased from certain financial institutions with maturities within one year. Our operating cash flow and cash are also affected by our ability to manage our inventory effectively and to enhance our overall supply chain efficiency. We believe that our supply chain and effective inventory management, which have resulted in reduced inventory turnover days, support the growing scale of our business, free our valuable working capital and improve our liquidity.

In September 2019, 1 Pharmacy Technology entered into a credit agreement with China Merchant Bank (CMB) which provides a revolving credit facility that allows 1 Pharmacy Technology to borrow up to RMB100,000 for working capital purposes in one year. In October 2020, 1 Pharmacy Technology renewed the credit agreement that allowed 1 Pharmacy Technology to borrow up to RMB300,000 for working capital purposes within one year. In November 2021, 1 Pharmacy Technology entered into a new credit agreement that allowed 1 Pharmacy Technology to borrow up to RMB300,000 for working capital purposes within one year. Any draw down on the credit facility will be charged with interest at one-year loan prime rate published by People's Bank of China plus 0.30%. The borrowings were guaranteed by Yihao Pharmacy. During the years ended December 31, 2020 and 2021, RMB229,666 and RMB331,837, respectively, were drawn on the above credit facility and RMB159,666 and RMB232,179, respectively, were repaid, with the balance of RMB100,000 and RMB199,658 outstanding as of December 31, 2020 and 2021, respectively. The interest rate range for the borrowings in 2020 and 2021 were from 4.10% to 4.35 % per annum.

In June 2020, 1 Pharmacy Technology entered into a credit agreement with Industrial Bank (IB) which provides a revolving credit facility that allows 1 Pharmacy Technology to borrow up to RMB100,000 for working capital purpose in one year. Any draw down on the credit facility will be charged with interest at one-year loan prime rate published by People's Bank of China minus 0.35%. In June 2021, the credit agreement was renewed and allows 1 Pharmacy Technology to borrow up to RMB200,000 for working capital purpose in seven months. Any draw down on the credit facility will be charged with interest at one-year loan prime rate published by People's Bank of China plus 0.78%. The borrowings in the years ended December 31, 2020 and 2021 were guaranteed by Yihao Pharmacy. During the years ended December 31, 2020 and 2021, RMB 9,850 and RMB 30,000 were drawn on this credit facility, RMB 9,850 were repaid in 2021, with the balance of RMB 9,850 and RMB 30,000 outstanding as of December 31, 2020 and 2021, respectively.

We entered into a revolving credit facility with China Zheshang Bank (CZB) that allows us to borrow up to RMB500,000 for working capital purposes since December 2018 and renewed in December 2020 which will expire in two years. Cash deposits or notes receivable are required to be pledged for any draw down of borrowings and notes payables from CZB. During 2020, Yihao Pharmacy repaid RMB65,081 borrowed from China Zheshang Bank (CZB) with no balance outstanding as of December 31, 2020. The interest rate for the borrowings in 2020 was 4.35% per annum. No loan with China Zheshang Bank (CZB) was entered in 2021. 1 Pharmacy Technology obtained a loan of RMB 40,000 from Shanghai Pudong Technology Financial Service Co., Ltd. with an annual interest rate of 8.5% in May 2020. The borrowing was guaranteed by Yihao Pharmacy. 1 Pharmacy Technology repaid RMB40,000 in 2021 with no balance outstanding as of December 31, 2021. 1 Pharmacy Technology also borrowed RMB10,000 from China Construction Bank (CCB) in 2020 and paid back in 2021. The loan agreement with CCB includes covenants that the debt to asset ratio of 1 Pharmacy Technology should be no more than 70%, and the liquidity ratio should be no less than 1.0. 1 Pharmacy Technology was in compliance with the covenants as of payment due date in 2021.

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We also obtained loans from several other financial institutions. During the years ended December 31, 2020 and 2021, RMB109,250 and RMB45,000 were borrowed, RMB39,850 and RMB84,400 were repaid, with the balance of RMB69,400 and RMB30,000 outstanding as of December 31, 2020 and 2021, respectively. The interest rate range for the borrowings was from 3.50% to 4.60% per annum in 2020 and 4.15 % to 4.60% per annum in 2021.

After considering all facts available to us as of the date of this annual report, we believe that our current cash and cash equivalents, short-term investments and our anticipated cash flows from operations will be sufficient to meet our anticipated working capital requirements and capital expenditures for the next 12 months.

We intend to finance our long-term working capital requirements and capital expenditures from cash generated from operating activities and funds raised from financing activities. We may, however, need additional capital in the future to fund our continued operations in light of the perceived or actual impact of COVID-19 pandemic on domestic and global economy. We may also need additional cash if 1 Pharmacy Technology's proposed listing on the STAR Market is not completed before June 30, 2023 or the date otherwise agreed, under which circumstance certain investors who are non-controlling shareholders of 1 Pharmacy Technology may require the controlling shareholder of 1 Pharmacy Technology, Yao Wang, to redeem all or part of the equity interests then owned by such investors in cash. If we determine that our cash requirements exceed the amount of cash and cash equivalents we have on hand at the time, we may seek to issue equity or debt securities or obtain credit facilities. The issuance and sale of additional equity or the incurrence of convertible debt would result in further dilution to our shareholders. The incurrence of indebtedness would result in increased fixed obligations and could result in operating covenants that might restrict our operations. We cannot assure you that financing will be available in amounts or on terms acceptable to us, if at all, and the availability of financing options will be affected by the slowdown in the growth or contraction of the global or Chinese economies or any liquidity or credit drainage in the global or Chinese finance sectors if triggered by the COVID-19 pandemic. See "Item 3. Key Information—D. Risk Factors—Risks Related to Our Business and Industry—We may need additional capital but may not be able to obtain it on favorable terms or at all."

Additionally, historically we have not been profitable or generated positive operating cash flows. We generated net loss of RMB467.1 million and RMB621.0 million (US\$97.5 million) in 2020 and 2021, respectively. We recorded net cash operating outflows of RMB116.8 million and RMB688.8 million (US\$108.1 million) in 2020 and 2021, respectively. If we are unable to achieve and sustain profitability, or if we continue to experience net cash operating outflows in the future, our business, liquidity, financial condition and results of operations may be materially and adversely affected. See "Item 3. Key Information—D. Risk Factors—Risks Related to Our Business and Our Industry—We have incurred operating losses in the past, and may not be able to achieve or maintain profitability in the future."

We expect that substantially all of our future net revenues will be denominated in Renminbi. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and trade and service-related foreign exchange transactions, can be made in foreign currencies without prior SAFE approval as long as certain routine procedural requirements are fulfilled. Therefore, our PRC subsidiary, 1 Pharmacy Technology, is allowed to pay dividends in foreign currencies to us without prior SAFE approval by following certain routine procedural requirements. However, approval from or registration with competent government authorities is required where the Renminbi is to be converted into foreign currency and remitted out of China to pay capital expenses such as the repayment of loans denominated in foreign currencies. The PRC government may at its discretion restrict access to foreign currencies for current account transactions in the future.

The following table sets forth material amounts of cash and short-term investments disaggregated by currency denomination as of December 31, 2021 in each jurisdiction in which our affiliated entities are domiciled:

	PRC	Hong Kong (RMB in thousands)	Cayman Islands
Cash and short-term investments in RMB	755,953	70	—
Cash and short-term investments in US\$	3,262	39,563	45,098

Cash Flows

The following table sets forth a summary of our cash flows for the years presented:

	For the Year Ended December 31,			
	2019	2020	2021	
	RMB	RMB	RMB	USS
Summary Consolidated Cash Flow Data:				
Net cash used in operating activities	(512,382)	(116,777)	(688,837)	(108,092)
Net cash provided by (used in) investing activities	237,675	(324,669)	60,138	9,437
Net cash provided by financing activities	108,987	1,070,407	74,339	11,665
Net (decrease) increase in cash and cash equivalents, and restricted cash	(156,018)	620,812	(557,862)	(87,540)
Cash and cash equivalents, and restricted cash at the beginning of period	853,740	697,722	1,318,534	206,907
Cash and cash equivalents, and restricted cash at the end of period	697,722	1,318,534	760,672	119,367

Operating Activities

Net cash used in operating activities in 2021 was RMB688.8 million (US\$108.1 million) and primarily consisted of our net loss of RMB621.0 million (US\$97.5 million), as adjusted for non-cash items and the effects of changes in operating assets and liabilities. Adjustment for non-cash items primarily included RMB145.6 million (US\$22.8 million) of share-based compensation, RMB46.0 million (US\$7.2 million) of inventory write-down and RMB89.8 million (US\$14.1 million) of noncash lease expense, partially offset by an increase in investment income of RMB7.8 million (US\$1.2 million). In 2021, the principal items accounting for the changes in operating assets and liabilities were increase in inventories of RMB400.6 million (US\$62.9 million), partially offset by an increase of RMB274.0 million (US\$43.0 million) in accounts payable and an increase in accrued expense and other current liabilities of RMB120.9 million (US\$19.0 million). The increases in accounts payable and inventory were primarily due to an increase in our inventory storage level to meet increased demands.

Net cash used in operating activities in 2020 was RMB116.8 million and primarily consisted of our net loss of RMB467.1 million, as adjusted for non-cash items and the effects of changes in operating assets and liabilities. Adjustment for non-cash items primarily included RMB75.7 million of share-based compensation, RMB24.2 million of inventory write-down and RMB39.3 million of noncash lease expense, partially offset by an increase in exchange loss of RMB5.5 million. In 2020, the principal items accounting for the changes in operating assets and liabilities were increase in inventories of RMB304.5 million, partially offset by an increase of RMB629.0 million in accounts payable and an increase in accrued expenses and other current liabilities of RMB111.3 million. The increases in accounts payable and inventory were primarily due to an increase in our inventory storage level to meet increased demands.

Net cash used in operating activities in 2019 was RMB512.4 million and primarily consisted of our net loss of RMB501.8 million, as adjusted for non-cash items and the effects of changes in operating assets and liabilities. Adjustment for non-cash items primarily included RMB54.3 million of share-based compensation expenses, RMB11.7 million of depreciation and amortization expenses and RMB11.0 million of investment loss and RMB25.4 million of noncash lease expense, partially offset by an increase in investment income of RMB9.6 million. In 2019, the principal items accounting for the changes in operating assets and liabilities were an increase in inventory of RMB276.2 million, partially offset by an increase of RMB232.1 million in accounts payable and an increase in accrued expenses and other current liabilities of RMB74.4 million. The increases in accounts payable and inventory were primarily due to an increase in our inventory storage level to meet increased demands.

Investing Activities

Net cash used in investing activities in 2021 was RMB60.1 million (US\$9.4 million), consisting primarily of purchases of short-term investments of RMB1,832.4 million (US\$287.5 million), partially offset by proceeds from sale or maturity of short-term investments of RMB1,957.8 million (US\$307.2 million).

Net cash used in investing activities in 2020 was RMB324.7 million, consisting primarily of purchases of short-term investments of RMB500.0 million, partially offset by proceeds from sale or maturity of short-term investments of RMB201.0 million.

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Net cash provided by investing activities in 2019 was RMB237.7 million, consisting primarily of proceeds from sale or maturity of short-term investments of RMB863.1 million, partially offset by purchases of short-term investments of RMB601.0 million.

Financing Activities

Net cash provided by financing activities in 2021 was RMB74.3 million (US\$11.7 million), consisting of proceeds from short-term bank borrowings of RMB406.8 million (US\$63.8 million), partially offset by repayment of short-term bank borrowings of RMB376.4 million (US\$59.1 million), and proceeds from reverse factoring arrangement of RMB61.9 million (US\$9.7 million), partially offset by repayment under reverse factoring arrangement of RMB15.0 million (US\$2.4 million).

Net cash provided by financing activities in 2020 was RMB1,070.4 million, consisting of proceeds from redeemable non-controlling shareholders of a subsidiary of RMB934.8 million, proceeds from short-term bank borrowings of RMB398.8 million, proceeds from non-controlling shareholders of a subsidiary of RMB32.5 million and proceeds from ordinary shareholders of RMB6.3 million, partially offset by repayment of short-term bank borrowings of RMB264.6 million, net proceeds used in other financing activities of RMB25.4 million and payment of share repurchase of RMB12.0 million.

Net cash provided by financing activities in 2019 was RMB109.0 million, consisting of proceeds from short-term bank borrowings of RMB150.9 million, net proceeds from issuance of other financing activities of RMB25.6 million and proceeds from ordinary shareholders of RMB11.3 million, partially offset by repayment of short-term bank borrowings of RMB55.8 million and payments for share repurchases of RMB23.0 million.

Material Cash Requirements

Our material cash requirements as of December 31, 2021 and any subsequent interim period primarily include our capital expenditures and operating lease commitments. We may also need additional cash if 1 Pharmacy Technology's proposed listing on the STAR Market is not completed before June 30, 2023 or the date otherwise agreed, under which circumstance certain investors who are non-controlling shareholders of 1 Pharmacy Technology may require the controlling shareholder of 1 Pharmacy Technology, Yao Wang, to redeem all or part of the equity interests then owned by such investors in cash. Other than those as discussed below, we did not have any significant capital and other commitments, long-term obligations or guarantees as of December 31, 2021. We did not have future minimum capital commitments as of December 31, 2019 and 2020 and 2021.

Capital Expenditures

We made capital expenditures of RMB24.6 million, RMB25.8 million and RMB65.7 million (US\$10.3 million) in 2019, 2020 and 2021, respectively. In these periods, our capital expenditures were primarily used for purchases of property, equipment and software to establish more fulfillment centers to meet the expected growth of our business.

Operating lease commitments

The following table sets forth our operating lease commitments as of December 31, 2021:

	Total	Less than 1 year (in RMB thousands)	1-3 years	3-5 years	More than 5 years
Operating lease commitments	249,466	73,723	126,565	48,973	205
Total	249,466	73,723	126,565	48,973	205

Our operating lease commitments relate to our leases of certain offices and fulfillment centers. Our lease expenses for the years ended December 31, 2019, 2020 and 2021 were RMB29.7 million, RMB41.9 million and RMB73.8 million (US\$11.6 million), respectively.

Off-Balance Sheet Commitments and Arrangements

We have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as shareholder's equity or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets

transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or product development services with us.

Holding Company Structure

111, Inc. is a holding company with no material operations of its own. We conduct our operations primarily through our PRC subsidiaries in China. As a result, 111, Inc.’s ability to pay dividends depends upon dividends paid by our PRC subsidiaries. If our existing PRC subsidiaries or any newly formed ones incur debt on their own behalf in the future, the instruments governing their debt may restrict their ability to pay dividends to us. In addition, 1 Pharmacy Technology, our subsidiary in China is permitted to pay dividends to us only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. Under PRC law, each of our PRC subsidiaries in China is required to set aside at least 10% of its after-tax profits each year, if any, to fund certain statutory reserve funds until such reserve funds reach 50% of their registered capital. In addition, our subsidiaries in China may allocate a portion of their after-tax profits based on PRC accounting standards to a surplus fund at their discretion. The statutory reserve funds and the discretionary funds are not distributable as cash dividends. Remittance of dividends by a foreign invested company out of China is subject to examination by the banks designated by SAFE. Our PRC subsidiary, 1 Pharmacy Technology, has not paid dividends and will not be able to pay dividends until they generate accumulated profits and meet the requirements for statutory reserve funds.

C. Research and Development, Patents and Licenses, etc.

See “Item 4. Information on the Company—B. Business Overview—Technology and IT Infrastructure” and “Item 4. Information on the Company—B. Business Overview—Intellectual Property.”

D. Trend Information

Other than as disclosed elsewhere in this annual report, we are not aware of any trends, uncertainties, demands, commitments or events for the year ended December 31, 2021 that are reasonably likely to have a material and adverse effect on our net revenues, income, profitability, liquidity or capital resources, or that would cause the disclosed financial information to be not necessarily indicative of future results of operations or financial conditions.

E. Critical Accounting Estimates

We prepare our consolidated financial statements in accordance with U.S. GAAP, which requires us to make judgments, estimates and assumptions that affect (1) the reported amounts of assets and liabilities, (2) disclosure of contingent assets and liabilities at the end of each reporting period, and (3) the reported amounts of revenues and expenses during each reporting period. We continually evaluate these estimates and assumptions based on historical experience, knowledge and assessment of current business and other conditions, and expectations regarding the future based on available information and reasonable assumptions, which together form a basis for making judgments about matters not readily apparent from other sources. Since the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates. Some of our accounting policies require higher degrees of judgment than others in their application. When reviewing our financial statements, you should consider (1) our selection of critical accounting policies, (2) the judgment and other uncertainties affecting the application of such policies, and (3) the sensitivity of reported results to changes in conditions and assumptions. We made the following critical accounting estimates to prepare our financial statements.

Fair value of ordinary shares of 1 Pharmacy

We granted restricted shares of 1 Pharmacy Technology to our employees under Employee ownership plan of 1 Pharmacy Technology. 1 Pharmacy Technology has been a private company with no active quoted market prices for its ordinary shares. We therefore needed to make estimates of the fair value of ordinary shares for the purpose of determining the fair value of restricted shares in 1 Pharmacy Technology at the date of the grant as one of the inputs. We estimate the fair value of the restricted shares at the date of grant in using income approach which requires that we prepare a forecast of future operations, as an input into the discounted cash flow model, which involves significant management judgment. Although management believes the Company's forecast is reasonable, no assurance can be given, especially when the Company is still in a loss making position. The discounted cash flows are sensitive due to changes in key forecast assumptions, including mainly revenue. The fair value of the shares granted during 2021 under Employee ownership plan of 1 Pharmacy Technology is RMB 67.5 million, which will be recognized over 4 years. If change in various factors constituting the estimate of revenue result in 5 percentage point increase/decrease in the overall estimate revenue, it would result in an increase/decrease of total compensation cost of RMB3.1/3.1million.

Item 6. Directors, Senior Management and Employees

A. Directors and Executive Officers

The following table sets forth information regarding our directors and executive officers as of the date of this annual report.

Directors and Executive Officers	Age	Position/Title
Gang Yu	62	Co-founder and Co-Chairman
Junling Liu	57	Co-founder, Co-Chairman and Chief Executive Officer
Lian Yong Chen	59	Director
Nee Chuan Teo	51	Independent Director
Jian Sun	57	Independent Director
Jun Luo	54	Independent Director

Dr. Gang Yu is our co-founder and has served as our executive chairman since 2015. Since September 2018, Dr. Yu has served as our co-chairman. Dr. Yu has over 23 years of experience in the technology sector and 14 years of experience in the e-commerce industry. He is a recipient of numerous prestigious international awards, including the 2002 Franz Edelman Management Science Achievement Award from INFORMS and the 2012 Martin K. Starr Excellence in Production and Operations Management Practice Award from POMS.

Dr. Yu co-founded and served as chairman of YHD.com, a leading e-commerce company in China. Dr. Yu currently serves as a director of Midea Group Co., Ltd. (SZSE: 000333), LightInTheBox Holding Co., Ltd. (NYSE: LITB) and Chindata Group Holdings Limited (NASDAQ: CD), and as the co-chairman of the board of Zall Group (02098.HK). Prior to founding YHD.com, Dr. Yu served as the vice president of Worldwide Procurement at Dell Inc. from 2006 to 2007 and the vice president of Worldwide Supply Chain at Amazon.com from 2004 to 2006. Before Amazon, Dr. Yu was the chair professor at McCombs School of Business at The University of Texas at Austin from 1989 to 2004. Dr. Yu received his bachelor's degree in science from Wuhan University in 1982, master's degree in physics from Cornell University in 1986 and Ph.D. degree in decision sciences from The Wharton School of the University of Pennsylvania in 1990. Dr. Yu has been a member of the Board of Overseers of The Wharton School of the University of Pennsylvania since 2019. Dr. Yu has published 6 books and over 80 journal articles. Dr. Yu also holds three U.S. patents related to airline optimization solutions.

Mr. Junling Liu is our co-founder and has served as our chairman and chief executive officer since 2015. Since September 2018, Mr. Liu has served as our co-chairman. He co-founded and served as chief executive officer of YHD.com from 2008 to 2015. Prior to founding YHD.com, Mr. Liu served as the global vice president and president for mainland China and Hong Kong at Dell Inc. from 2006 to 2007. He also held numerous executive positions at internationally renowned technology companies such as Avaya China, Openwave Systems and Lucent Technologies Asia. Since January 2015, he has been an independent director of Autohome Inc. (NYSE: ATHM), the leading online destination for automobile consumers. Mr. Liu also serves as an independent director of Hua Medicine (02552.HK). Mr. Liu received his bachelor's degree in education from Flinders University in Australia in 1991 and master's degree in international business administration from Flinders University in 1998.

Dr. Lian Yong Chen has served as our director since May 2019. He is currently the founding managing partner and CEO of 6 Dimensions Capital. He has over 20 years of experience in the life sciences industry in China and the United States as a venture capitalist, senior management executive, entrepreneur, and scientific inventor. He was the founder and managing partner at Frontline

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Bio Ventures and a partner at FIL Capital Management (Hong Kong) Limited in Asia from May 2008 to March 2014. Dr. Chen has been an executive director and the chairman of the board of Ocumension Therapeutics since May 2018, a company listed on the Stock Exchange (stock code: 1477). Since August 2018 to July 2021, he has served as a director at CStone Pharmaceuticals, a company listed on the main board of the Stock Exchange (stock code: 2616). Since May 2018, he has served as a non-executive Director at Hua Medicine, a company listed on the main board of the Stock Exchange (stock code: 2552). He served as a director of Shanghai Hile Bio-Pharmaceutical Co. Ltd., a company listed on the Shanghai Stock Exchange (stock code: 603718) since December 2014 to May 2021. Save as disclosed above, Dr. Lian Yong Chen is not and has not been a director of any other listed companies in the past three years. Dr. Lian Yong Chen conducted postdoctoral research at the Massachusetts Institute of Technology after obtaining his Ph.D. degree in Chemistry (with top honor) from the University of Louvain, Louvain-La-Neuve in Belgium in July 1991. He obtained his Bachelor of Science degree in Chemistry from Peking University in June 1984.

Mr. Nee Chuan Teo has served as our independent director since September 2018. Mr. Teo is the chief financial officer of bioduro-sundia, a famous company providing its biopharma customers a single end-to-end solution from early stage drug discovery to late stage manufacturing. Prior to joining bioduro-sundia, Mr. Teo served as chief financial officer of Huazhu Group Limited (formerly China Lodging Group Limited, Nasdaq: HTHT), a leading fast-growing multi-brand hotel group in China from 2015 to 2021. He also served as chief financial officer of Rnomac International Group, the largest Volvo construction equipment distributor in China, from 2011 to 2015; and served as financial controller in Focus Media Group from 2007 to 2009. Mr. Teo received his bachelor of science in accounting and financial analysis from Warwick University, the United Kingdom. He is a chartered certified accountant in the United Kingdom and a certified public accountant in the United States and Hong Kong..

Mr. Jian Sun has served as our independent director since September 2018. Mr. Sun is an executive director and the general manager of BTG Hotels (Group) Co., Ltd. (Shanghai Stock Exchange Stock Code: 600258), a top tourism service company in China. Prior to joining BTG Hotels Group, Mr. Sun served as executive director and chief executive officer of Home Inns Group, a leading economy hotel chain in China previously listed on Nasdaq, from 2004 to 2016. From 2010 to 2014, Mr. Sun served as independent director, chairman of the compensation committee and a member of the audit committee of Mecox Lane Limited, an online platform for apparel and accessories listed on Nasdaq. Since 2014, Mr. Sun has served as an independent director and a member of the compensation committee of two companies listed on the New York Stock Exchange, including Leju Holdings Limited, a leading online-to-offline real estate services provider in China, and eHi Car Services Limited, a leading car services and car rental provider in China. Mr. Sun holds a bachelor's degree from Shanghai Medical University in China.

Mr. Jun Luo has served as our independent director since September 2018. Mr. Luo is the co-founder and chief executive officer of Tujia & Sweetome Group, a leading short-term property rental firm in China. Prior to co-founding Tujia & Sweetome Group, Mr. Luo served as general manager of Shanghai SINA Leju and executive president at China Real Estate Information Corporation. Mr. Luo received his bachelor's degree in accounting from Shanghai University of Finance and Economics in 1994 and master's degree in software engineering from Beihang University in China in 2010.

B. Compensation

For the year ended December 31, 2021, we paid an aggregate of approximately RMB9.3 million (US\$1.5 million) in cash and other benefits to our directors and executive officers. For share incentive grants to our officers and directors, see “—Share Incentives.” We have not set aside or accrued any amount to provide pension, retirement or other similar benefits to our executive officers and directors. Our PRC subsidiaries are required by law to make contributions equal to certain percentages of each employee's salary for his or her pension insurance, medical insurance, unemployment insurance and other statutory benefits and a housing provident fund.

Share Incentives

Share Incentive Policies

We adopted certain share incentive policies in December 2013 and August 2014, or the 2013 Policy and the 2014 Policy, respectively, for the purpose of granting share based compensation awards to our officers, employees, directors, consultants and other eligible persons to incentivize their performance and promote the success of our business.

Share Incentive Plans

2016 Plan

We adopted our 2016 Share Incentive Plan, or the 2016 Plan, in January 2016, to promote our success and the interests of our shareholders by providing a means through which we may grant equity-based incentives to attract, motivate, retain and reward certain officers, employees, directors, consultants and other eligible persons to further link the interests of recipients with those of our shareholders generally. Since the adoption of the 2016 Plan, we stopped granting awards under the 2013 Policy or the 2014 Policy, although the outstanding awards under the 2013 Policy and the 2014 Policy are still being administered under their respective policies.

The following paragraphs summarize the terms of the 2016 Plan.

Types of Awards. The 2016 Plan permits awards of options, share appreciation rights, restricted shares and restricted share units.

Plan Administration. The 2016 Plan will be administered by our board of directors or by a committee designated by our board of directors. The committee or the full board of directors, as applicable, will determine the participants to receive awards, the type and number of awards to be granted to each participant, and the terms and conditions of each award grant.

Award Agreement. Generally, awards granted under the 2016 Plan are evidenced by an award agreement that sets forth terms, conditions and limitations for each award, which must be consistent with the plan.

Exercise Price. The plan administrator determines the exercise price for each award, which is stated in the award agreement.

Eligibility. We may grant awards only to those persons that the plan administrator determines to be eligible persons, which may include our employees, directors and consultants.

Term of the Awards. The term of each award granted under the 2016 Plan may not exceed ten years from the date of the grant.

Vesting Schedule. In general, the plan administrator determines the vesting schedule, which is set forth in the award agreement.

Acceleration of Awards upon Change in Control. The plan administrator may determine, at the time of grant or thereafter, that an award will become vested and exercisable, in full or in part, in the event that a change in control of our company occurs.

Transfer Restrictions. Awards may not be transferred in any manner by the recipient other than by will or the laws of descent and distribution, except as otherwise provided by the plan administrator.

Termination. Unless terminated earlier, the 2016 Plan has a term of fifteen years.

Under the 2013 Policy, the 2014 Policy and the 2016 Plan, the maximum aggregate number of shares which may be issued pursuant to all awards is 13,671,109 ordinary shares. As of the date of this annual report, options to purchase a total of 7,212,287 ordinary shares and 60,000 restricted share units were granted and outstanding under the 2013 Policy, the 2014 Policy and the 2016 Plan.

2018 Plan

In August 2018, we adopted our 2018 Share Incentive Plan, or the 2018 Plan, which became effective on September 15, 2018, one day after the completion of our initial public offering, replacing the 2016 Plan in its entirety. The 2018 Plan allows us to offer share-based incentive awards to employees, officers, directors and individual consultants who render services to us. The 2018 Plan permits the grant of options, restricted shares and restricted share units, or other types of awards, in the form of cash or otherwise, as approved by our board of directors or a committee thereof. The maximum number of Class A ordinary shares that may be issued pursuant to all awards under the 2018 Plan is 13,671,109, plus an annual increase on the first day of each fiscal year of our company during the ten-year term of the 2018 Plan commencing with the fiscal year beginning January 1, 2019, by an amount equal to the lesser of (i) 1.0% of the total number of shares issued and outstanding on the last day of the immediately preceding fiscal year, and (ii) such number of shares as may be determined by our board of directors. Upon the effectiveness of the 2018 Plan, we no longer grant any awards under the 2016 Plan. Outstanding awards granted under the 2016 Plan will remain effective and be subject to the terms

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and conditions of the 2018 Plan. As of the date of this annual report, options to purchase a total of 2,232,198 Class A ordinary shares and 4,175,604 restricted share units were granted and outstanding under the 2018 Plan. The following paragraphs summarize the terms of the 2018 Plan:

Plan Administration. Our board of directors, or a committee designated by our board of directors, will administer the plan. The plan administration committee will determine the provisions and terms and conditions of each grant.

Award Agreements. Options and other awards granted under the plan are evidenced by an award agreement that sets forth the terms, conditions and limitations for each grant, which may include the term of the award and the provisions applicable in the event the grantee's employment or service terminates.

Exercise Price. The exercise price of an option will be determined by the plan administration committee, which may be a fixed price or a variable price related to the fair market value on the grant date of the respective option. The exercise price of granted options may be amended or adjusted in the absolute discretion of the plan administration committee without the approval of our shareholders or the recipients of the options.

Eligibility. We may grant awards to employees, directors and consultants of our company and our majority-owned subsidiaries as determined by the plan administration committee.

Vesting Schedule. In general, the plan administration committee determines the vesting schedule, which is specified in the relevant award agreement.

Acceleration of Awards upon Change in Control. If a change-of-control corporate transaction occurs, the plan administration committee may, in its sole discretion, provide for (i) all awards outstanding to terminate at a specific time in the future and give each participant the right to exercise the vested portion of such awards during a specific period of time, or (ii) the purchase of any award for an amount of cash equal to the amount that could have been attained upon the exercise of such award, or (iii) the replacement of such award with other rights or property selected by the plan administration committee in its sole discretion, or (iv) payment of award in cash based on the value of ordinary shares on the date of the change-of-control corporate transaction plus reasonable interest.

Term of the Options. The term of each option grant shall be stated in the award agreement, provided that the term shall not exceed ten years from the date of the grant.

Transfer Restrictions. Subject to certain exceptions, awards may not be transferred by the recipient.

Termination of the Plan. The 2018 Plan shall terminate in 2028, provided that our board of directors may terminate the plan at any time and for any reason.

Our Employee Share Holding Platform

In November 2014, we established Gold Prized Investment Limited, or Gold Prized, a company incorporated in the British Virgin Islands, as an offshore employee shareholding platform to allow our employees in China to receive share incentives.

Gold Prized is wholly owned by Shanghai Yiyao Enterprise Management Partners, or Yiyao Partners, a limited partnership formed in the PRC and owned by Ms. Jing Liu (0.81%), a family member of Mr. Junling Liu, and Ms. Ying Song (99.19%), a family member of Dr. Gang Yu. Ms. Ying Song is the general partner while Ms. Jing Liu is the sole limited partner of Yiyao Partners.

We issued class C ordinary shares to Gold Prized, and did not grant any rights associated with the class C ordinary shares held by Gold Prized to our directors and executive officers or any other employees. We have transferred the class C ordinary shares issued to Gold Prized back to our company and have reserved those shares for the 2016 Plan. Gold Prized has since ceased to be a shareholder of our company.

1 Pharmacy Technology Share Incentive Plan

In November 2020, our subsidiary, 1 Pharmacy Technology issued 32,500,000 ordinary shares to 13 limited liability partnerships ("LLPs") founded by the employees of 1 Pharmacy Technology with the total consideration of RMB32.5 million. The shares issued to

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the employees in each LLP are not outstanding shares but are restricted with 50% of the shares vesting within two years from the issuance date and the remaining 50% vesting evenly on an annual basis over the two years thereafter, which are also subject to adjustment based on performance condition. Such arrangement was entered into to provide a share incentive plan to the employees of 1 Pharmacy Technology. For more details, see Notes 13 and 15 to our consolidated financial statements included elsewhere in this annual report.

The following table summarizes, as of the date of this annual report, the outstanding share incentive awards we have granted to our directors and executive officers under the 2013 Policy, the 2014 Policy, the 2016 Plan and the 2018 Plan:

Name	Ordinary Shares Underlying Outstanding Share Incentive Awards	Exercise Price (\$/Share)	Grant Date	Expiration Date
		4/13/2020	4/12/2030	
		5/13/2020	5/12/2030	
		6/13/2020	6/12/2030	
		7/13/2020 and	7/12/2030	
Gang Yu	*	†	1/1/2021	12/31/2030
		4/13/2020	4/12/2030	
		5/13/2020	5/12/2030	
		6/13/2020 and	6/12/2030	
		7/13/2020	7/12/2030	
Junling Liu	*	†	5/13/2020	5/12/2030
Lian Yong Chen	*	†	6/1/2019	5/31/2029
Nee Chuan Teo	*	†	9/12/2018	9/11/2028
Jian Sun	*	†	9/12/2018	9/11/2028
Jun Luo	*	†	9/12/2018	9/11/2028
All directors and executive officers as a group	127,290			

* Less than one percent of our total outstanding shares.

† Restricted share units.

C. Board Practices

Board of Directors

Our board of directors consists of six directors. A director is not required to hold any shares in our company to qualify to serve as a director. A director who is in any way, whether directly or indirectly, interested in a contract or transaction or proposed contract or transaction with our company is required to declare the nature of his interest at a meeting of our directors. A director may vote with respect to any contract or transaction or proposed contract or transaction notwithstanding that he may be interested therein, and if he does so his vote shall be counted and he may be counted in the quorum at any meeting of our directors at which any such contract or transaction is considered. Our directors may exercise all the powers of our company to borrow money, mortgage or charge its undertaking, property and uncalled capital and to issue debentures or other securities whenever money is borrowed or as security for any debt, liability or obligation of our company or of any third party.

Committees of the Board of Directors

We have three committees under the board of directors: an audit committee, a compensation committee and a nominating and corporate governance committee. We have adopted a charter for each of the three committees. Each committee's members and functions are described below.

Audit Committee

Our audit committee consists of Nee Chuan Teo, Jian Sun and Jun Luo, and is chaired by Nee Chuan Teo. Nee Chuan Teo, Jian Sun and Jun Luo each satisfies the “independence” requirements of Rule 5605(c)(2) of the Nasdaq Stock Market Rules and meet the independence standards under Rule 10A-3 under the Exchange Act. We have determined that Nee Chuan Teo qualifies as an “audit committee financial expert.” The audit committee oversees our accounting and financial reporting processes and the audits of the financial statements of our company. The audit committee is responsible for, among other things:

- selecting the independent registered public accounting firm and pre-approving all auditing and non-auditing services permitted to be performed by the independent registered public accounting firm;
- reviewing with the independent auditors any audit problems or difficulties and management’s response;
- reviewing and approving all proposed related party transactions, as defined in Item 404 of Regulation S-K under the Securities Act;
- discussing the annual audited financial statements with management and the independent registered public accounting firm;
- reviewing major issues as to the adequacy of our internal controls and any special audit steps adopted in light of material control deficiencies;
- annually reviewing and reassessing the adequacy of our audit committee charter;
- meeting separately and periodically with management and the independent registered public accounting firm; and
- reporting regularly to the board.

Compensation Committee

Our compensation committee consists of Gang Yu, Nee Chuan Teo and Jian Sun, and is chaired by Gang Yu. Nee Chuan Teo and Jian Sun each satisfies the “independence” requirements of Rule 5605(a)(2) of the Nasdaq Stock Market Rules. The compensation committee assists the board in reviewing and approving the compensation structure, including all forms of compensation, relating to our directors and executive officers. Our chief executive officer may not be present at any committee meeting during which his compensation is deliberated upon. The compensation committee is responsible for, among other things:

- reviewing the total compensation package for our executive officers and making recommendations to the board with respect to it;
- reviewing the compensation of our non-employee directors and making recommendations to the board with respect to it; and
- periodically reviewing and approving any long-term incentive compensation or equity plans, programs or similar arrangements, annual bonuses, and employee pension and welfare benefit plans.

Nominating and Corporate Governance Committee

Our nominating and corporate governance committee consists of Junling Liu, Jian Sun and Jun Luo, and is chaired by Junling Liu. Jian Sun and Jun Luo each satisfies the “independence” requirements of Rule 5605(a)(2) of the Nasdaq Stock Market Rules. The nominating and corporate governance committee assists the board in selecting individuals qualified to become our directors and in determining the composition of the board and its committees. The nominating and corporate governance committee is responsible for, among other things:

- recommending nominees to the board for election or re-election to the board, or for appointment to fill any vacancy on the board;

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- reviewing annually with the board the current composition of the board with regards to characteristics such as independence, age, skills, experience and availability of service to us;
- selecting and recommending to the board the names of directors to serve as members of the audit committee and the compensation committee, as well as of the nominating and corporate governance committee itself; and
- monitoring compliance with our code of business conduct and ethics, including reviewing the adequacy and effectiveness of our procedures to ensure proper compliance.

Terms of Directors and Executive Officers

Our board of directors may, by the affirmative vote of a simple majority of the remaining directors present and voting at a meeting of our board, which shall include the affirmative vote of at least one Founder as long as either Founder is a director, appoint any person as a director, to fill a vacancy on the board arising from the office of any director being vacated. Our shareholders may also appoint any person to be a director by way of ordinary resolution. Our directors are not subject to a term of office and hold office until such time as they are removed from office by ordinary resolution of the shareholders. A director will cease to be a director if, among other things, the director (i) becomes bankrupt or makes any arrangement or composition with his creditors; (ii) dies or is found by our company to be or becomes of unsound mind, (iii) resigns his office by notice in writing to the company, or (iv) without special leave of absence from our board, is absent from three consecutive board meetings and our directors resolve that his office be vacated.

Our founders serve as co-chairmen of our board of directors. For so long as each of our founders is a director of our company, he shall be a co-chairman of our board of directors, until he resigns as co-chairman or ceases to be a director (in which event he shall automatically cease to be a co-chairman). If either founder ceases to be a co-chairman, the other founder shall continue as the sole chairman of our board (unless our board, with the consent of the other founder, elects and appoints another director to be another co-chairman). Upon both founders ceasing to be co-chairmen or chairman, our board shall elect and appoint the co-chairmen or chairman at their discretion.

Subject to the foregoing, our officers are elected by and serve at the discretion of our board of directors.

Employment Agreements and Indemnification Agreements

We have entered into employment agreements with our senior executive officers. Pursuant to these agreements, we are entitled to terminate a senior executive officer's employment for cause at any time without remuneration for certain acts of the officer, such as being convicted of any criminal conduct, any act of gross or willful misconduct or any serious, willful, grossly negligent or persistent breach of any employment agreement provision, or engaging in any conduct which may make the continued employment of such officer detrimental to our company. In connection with the employment agreements, each senior executive officer agrees to hold all information, know-how and records in any way connected with the products of our company, including, without limitation, all software and computer formulas, designs, specifications, drawings, data, manuals and instructions and all customer and supplier lists, sales and financial information, business plans and forecasts, all technical solutions and the trade secrets of our company, in strict confidence perpetually. Each officer also agrees that we shall own all the intellectual property developed by such officer during his or her employment.

We have entered into indemnification agreements with each of our directors and executive officers. Under these agreements, we agree to indemnify them against certain liabilities and to reimburse them for expenses in connection with claims made by reason of their being a director or officer of our company.

Board Diversity

We value and consider broad diversity for our Board, including ethnicity, gender, nationality and age. The table below provides certain information regarding the diversity of our board of directors as of the date of this report. Each of the categories listed in the below table has the meaning as it is used in Nasdaq Rule 5605(f) and related instructions.

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Board Diversity Matrix (As of March 31, 2022)				
Country of Principal Executive Offices:	People's Republic of China			
Foreign Private Issuer	Yes			
Disclosure Prohibited Under Home Country Law	No			
Total Number of Directors	6			
	Female	Male	Non-Binary	Did Not Disclose Gender
Part I: Gender Identity				
Directors	0	6	0	0
Part II: Demographic Background				
Underrepresented Individual in Home Country Jurisdiction	1			
LGBTQ+	0			
Did Not Disclose Demographic Background	0			

D. Employees

The following table sets forth the numbers of our employees categorized by function as of December 31, 2021.

Functions:	As of December 31, 2021	
	Number	% of Total
Wholesale pharmacy business	1,084	51.3
Retail pharmacy business	226	10.7
Supply chain	187	8.8
Procurement	207	9.8
Research and development and IT	295	14.0
General and administrative	115	5.4
Total	2,114	100.0

As required by laws and regulations in China, we participate in various employee social security plans that are organized by municipal and provincial governments including, among other things, pension, medical insurance, unemployment insurance, maternity insurance, on-the-job injury insurance and housing fund plans through a PRC government-mandated benefit contribution plan. We are required under PRC law to make contributions to employee benefit plans at specified percentages of the salaries, bonuses and certain allowances of our employees, up to a maximum amount specified by the local government from time to time.

We typically enter into standard employment agreements and confidentiality agreements or clauses with our senior management and core personnel. These contracts include a standard non-compete covenant that prohibits the employee from competing with us, directly or indirectly, during his or her employment and for two years after termination of his or her employment.

We maintain a good working relationship with our employees and the labor union in Guangzhou, and we have not experienced any material labor disputes.

E. Share Ownership

The following table sets forth information with respect to the beneficial ownership of our shares as of March 31, 2022 by:

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

The calculations in the table below are based on 166,543,166 ordinary shares outstanding as of March 31, 2022, comprising of (i) 94,543,166 Class A ordinary shares, and (ii) 72,000,000 Class B ordinary shares.

Beneficial ownership is determined in accordance with the rules and regulations of the SEC. In computing the number of shares beneficially owned by a person and the percentage ownership of that person, we have included shares that the person has the right to acquire within 60 days after March 31, 2022, including through the exercise of any option, warrant or other right or the conversion of any other security. These shares, however, are not included in the computation of the percentage ownership of any other person.

	Class A Ordinary Shares	Class B Ordinary Shares	Percentage of total ordinary shares on an as-converted basis	Percentage of aggregate voting power†
Directors and Executive Officers: *				
Gang Yu ⁽¹⁾⁽⁹⁾	**	36,000,000	21.6	46.0
Junling Liu ⁽²⁾⁽⁷⁾	1,074,241	36,000,000	22.3	46.1
Lian Yong Chen ⁽³⁾	—	—	—	—
Nee Chuan Teo ⁽⁴⁾	**	—	**	**
Jian Sun ⁽⁵⁾	**	—	**	**
Jun Luo ⁽⁶⁾	—	—	—	—
All directors and executive officers as a group	1,111,219	72,000,000	43.9	92.0
Principal Shareholders:				
Sunny Bay Global Limited ⁽⁷⁾	—	36,000,000	21.6	46.0
ClearVue Partners, L.P. ⁽⁸⁾	17,063,470	—	10.2	1.5
Infinity Cosmo Limited ⁽⁹⁾	—	11,494,252	6.9	14.7
First Pharmacia International ⁽¹⁰⁾	8,690,562	—	5.2	0.7

Notes:

* Except for Dr. Lian Yong Chen, Mr. Nee Chuan Teo, Mr. Jian Sun and Mr. Jun Luo, the business address of our directors and executive officers is 3-5/F, No. 295 ZuChongZhi Road, Pudong New Area, Shanghai, the People's Republic of China.

** Less than 1% of our total outstanding shares.

† For each person or group included in this column, percentage of aggregate voting power represents voting power based on both Class A and Class B ordinary shares held by such person or group with respect to all outstanding shares of our Class A and Class B ordinary shares as a single class. Each holder of our Class A ordinary shares is entitled to one vote per share. Each holder of our Class B ordinary shares is entitled to fifteen votes per share. Our Class B ordinary shares are convertible at any time by the holder into Class A ordinary shares on a one-for-one basis.

- (1) Represents 24,505,748 Class B ordinary shares held by Dr. Gang Yu, and 11,494,252 Class B ordinary shares held by Infinity Cosmo Limited, a company incorporated in the British Virgin Islands. Infinity Cosmo Limited is controlled by Gang Yu Irrevocable Trust.
- (2) Represents 1,074,241 Class A ordinary shares held by Mr. Junling Liu and 36,000,000 Class B ordinary shares held by Sunny Bay Global Limited, a company incorporated in the British Virgin Islands. Sunny Bay Global Limited is wholly owned by Mr. Liu.

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- (3) The business address of Dr. Lian Yong Chen is Block 6, No. 999 Huanke Road, Pudong New District, Shanghai, China.
- (4) The business address of Mr. Nee Chuan Teo is 2201, Block 31, 388 Furongjiang Road, Shanghai, China.
- (5) The business address of Mr. Jian Sun is 124 Caobao Road, Xuhui District, Shanghai, China.
- (6) The business address of Mr. Jun Luo is Floor 3, 6B Tower, Huan Ya Technology Building, Lane 1228, Jiang Chang Road, Jing'an District, Shanghai, China.
- (7) Represents 36,000,000 Class B ordinary shares held by Sunny Bay Global Limited, a company incorporated in the British Virgin Islands. Sunny Bay Global Limited is wholly owned by Mr. Junling Liu. The registered office address of Sunny Bay Global Limited is Vistra Corporate Services Centre, Wickhams Cay II, Road Town, Tortola, VG1110, British Virgin Islands.
- (8) Represents (i) 8,531,231 ADSs (representing 17,062,462 Class A ordinary shares) held by ClearVue YW Holdings, Ltd., and (ii) 504 ADSs (representing 1,008 Class A ordinary shares) held by ClearVue Partners, L.P. ClearVue YW Holdings, Ltd. is wholly owned by ClearVue Partners, L.P., and as such, ClearVue Partners, L.P. may exercise voting and dispositive power over these shares held by ClearVue YW Holdings, Ltd. ClearVue Partners GP, L.P. is the general partner of ClearVue Partners, L.P., and as such, may exercise voting and dispositive power over the shares held by ClearVue YW Holdings, Ltd. by way of ClearVue Partners, L.P. and the shares held by ClearVue Partners, L.P. ClearVue Partners Ltd. is the general partner of ClearVue Partners GP, L.P., and as such, may exercise voting and dispositive power over the shares held by ClearVue YW Holdings, Ltd. and ClearVue Partners, L.P. by way of ClearVue Partners GP, L.P. The registered office address of ClearVue Partners, L.P. is Harneys Fiduciary (Cayman) Limited, 4th Floor, Harbour Place, 103 South Church Street, P.O. Box 10240, Grand Cayman KY1-1002, Cayman Islands.
- (9) Represents 11,494,252 Class B ordinary shares held by Infinity Cosmo Limited, a company incorporated in the British Virgin Islands. Infinity Cosmo Limited is controlled by Gang Yu Irrevocable Trust, a trust managed by Zedra Asia Limited, as the trustee. Dr. Gang Yu is the settlor of the Gang Yu Irrevocable Trust, and Dr. Yu's family members are the trust's beneficiaries. Under the terms of this trust, a family member of Gang Yu has the power to direct the trustee with respect to the disposal of, and the exercise of any voting and other rights attached to, the shares held by Infinity Cosmo Limited in our company. The registered office address of Infinity Cosmo Limited is Sertus Chambers, P.O. Box 905, Quastisky Building, Road Town, Tortola, British Virgin Islands.
- (10) Represents 4,345,281 ADSs (representing 8,690,562 Class A ordinary shares) directly held by First Pharmacia International, a Cayman Islands exempted company. First Pharmacia International is held by BVCF III L.P. (92.38%) and BVCF III-A L.P. (7.62%), each a Cayman Islands exempted limited partnership. The registered office address of First Pharmacia International is Walkers Corporate Limited, Cayman Corporate Centre, 27 Hospital Road, George Town, Grand Cayman, KY1-9008, Cayman Islands.

Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of Class A ordinary shares are entitled to one vote per share, while holders of Class B ordinary shares are entitled to fifteen votes per share. We issued Class A ordinary shares represented by the ADSs in our initial public offering in September 2018. Holders of our Class B ordinary shares may choose to convert their Class B ordinary shares into the same number of Class A ordinary shares at any time. Class A ordinary shares are not convertible into Class B ordinary shares under any circumstance.

To our knowledge, as of March 31, 2022, a total of 119,442,514 ordinary shares, representing approximately 71.7% of our total outstanding ordinary shares, were held by two record shareholders in the United States, including The Bank of New York Mellon, the depositary of our ADS program. The number of beneficial owners of our ADSs in the United States is likely to be much larger than the number of record holders of our ordinary shares in the United States.

Except for the above, we are not aware of any arrangement that may, at a subsequent date, result in a change of control of our company.

Item 7. Major Shareholders and Related Party Transactions

A. Major Shareholders

Please refer to "Item 6. Directors, Senior Management and Employees—E. Share Ownership."

B. Related Party Transactions

Termination of Contractual Arrangements with Variable Interest Entities

On January 27, 2022, 1 Pharmacy Technology entered into (1) a termination agreement with Yihao Pharmacy, Mr. Yue Xuan and Ms. Jing Liu, who were the shareholders of Yihao Pharmacy, (2) a termination agreement with Yihao Pharmaceutical Chain and Yihao Pharmacy, (3) a termination agreement with Shanghai Yaowang and Yihao Pharmaceutical Chain. Yihao Pharmacy, Yihao Pharmaceutical Chain and Shanghai Yaowang were all the VIEs that were subject to the contractual arrangements. On January 27, 2022, 1 Pharmacy Technology entered into a share transfer agreement with Mr. Yue Xuan and Ms. Jing Liu. As a result, 1 Pharmacy Technology currently holds 100% of equity interest in Yihao Pharmacy, and we operate our relevant business through our subsidiaries incorporated in the PRC.

Shareholders Agreement

We entered into our tenth amended and restated shareholders agreement on June 19, 2018 with our then-existing shareholders. The shareholders agreement provides for board representation rights to certain shareholders, which terminated upon our initial public offering. The shareholders agreement also provides for certain information and inspection rights, board observer rights, preferential rights, including right of participation, right of first refusal, co-sale rights and redemption rights. All information and inspection rights and preferential rights terminated upon our initial public offering.

Registration Rights

Pursuant to our current shareholders agreement, we have granted certain registration rights to our shareholders. Set forth below is a description of the registration rights granted under the agreement.

Demand Registration Rights. At any time after six months following a QIPO as defined in the shareholders agreement, holders of at least 25% of our registrable securities have the right to demand in writing that we file a registration statement covering the registration of their registrable securities. We have the right to defer filing of a registration statement for a period of not more than 90 days if our board of directors determines in good faith that filing of a registration statement in the near future will be materially detrimental to us and our shareholders, but we cannot exercise the deferral right more than once during any twelve-month period. We are not obligated to effect more than two demand registrations. Further, if the registrable securities are offered by means of an underwritten offering, and the underwriters advise us in writing that marketing factors require a limitation of the number of share to be underwritten, the underwriters may reduce as required and allocate the shares to be included in the registration statement among holders of our registrable securities on a pro rata basis, subject to certain limitations.

Piggyback Registration Rights. If we propose to file a registration statement for a public offering of our securities, we must offer holders of our registrable securities an opportunity to be included in such registration. If the underwriters determine in good faith that marketing factors require a limitation of the number of shares to be underwritten, the registrable securities shall allocate first to us, second, to each holder of our registrable securities requesting inclusion of their registrable securities pursuant to the piggyback registration, on a pro rata basis, and third, to other holders of our securities.

Form F-3 or Form S-3 Registration Rights. After our initial public offering, we shall use our best efforts to qualify for registration on Form F-3 or Form S-3. Holders of 10% or more of our registrable securities may request us in writing to file a registration statement on Form F-3 or Form S-3 if we qualify for registration on such forms, subject to certain limitations. We have the right to defer filing for a period of not more than 60 days if our board of directors determines in good faith that effecting registration at such time would be materially detrimental to us and our shareholders, but we cannot exercise the deferral right more than once during any twelve-month period, and we may not register any of our other shares during such 60-day period. The holders of our registrable securities are entitled to an unlimited number of registrations on Form F-3 or Form S-3. We, however, are not obligated to effect such registration if we have effected two such registrations within any twelve-month period.

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Expenses of Registration. We will bear all registration expenses, other than underwriting discounts and selling commissions applicable to the sale of registrable securities, incurred in connection with registrations, filings or qualification pursuant to the shareholders agreement. We will not be required to pay for any expenses of any registration proceeding begun pursuant to demand registration rights, unless subject to certain exception, if the registration request is subsequently withdrawn at the request of a majority of the holders of the registrable securities to be registered.

Termination of Obligations. We have no obligation to effect any demand, piggyback or Form F-3 or Form S-3 registration upon the earlier of (i) the fifth anniversary from the date of closing of a QIPO, (ii) a Trade Sale as defined in the shareholders agreement, and (iii) with respect to any holder of our registrable securities, the date following a QIPO on which such holder holds less than 1% of our total outstanding share capital.

Employment Agreements and Indemnification Agreements

See “ Item 6—Directors, Senior Management and Employees—C. Board Practices”

Share Incentive Plans

See “ Item 6. Directors, Senior Management and Employees—B. Compensation”

C. Interests of Experts and Counsel

Not applicable.

Item 8. Financial Information

A. Consolidated Statements and Other Financial Information

We have appended consolidated financial statements filed as part of this annual report.

Legal Proceedings

We are currently not a party to any material legal or administrative proceedings. We may from time to time be subject to various legal or administrative claims and proceedings arising in the ordinary course of business. Litigation or any other legal or administrative proceeding, regardless of the outcome, is likely to result in substantial cost and diversion of our resources, including our management’s time and attention.

Dividend Policy

We have not previously declared or paid cash dividends and we have no plan to declare or pay any dividends in the near future on our shares. We currently intend to retain most, if not all, of our available funds and any future earnings to operate and expand our business.

We are a holding company incorporated in the Cayman Islands. We rely principally on dividends from our PRC subsidiaries for our cash requirements, including any payment of dividends to our shareholders. PRC regulations may restrict the ability of our PRC subsidiaries to pay dividends to us. See “Item 3. Key Information—D. Risk Factors—Risks Related to Doing Business in China—We rely on dividends and other distributions on equity paid by our PRC subsidiaries to fund any cash and financing requirements we may have, and any limitation on the ability of our PRC subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our business.”

Our board of directors has discretion as to whether to distribute dividends, subject to certain restrictions under Cayman Islands law, namely that our company may only pay dividends either out of profits or share premium account, and provided always that in no circumstances may a dividend be paid if this would result in our company being unable to pay its debts as they fall due in the ordinary course of business. In addition, our shareholders may by ordinary resolution declare a dividend, but no dividend may exceed the amount recommended by our board of directors. Even if our board of directors decides to pay dividends, the form, frequency and

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amount will depend upon our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors that the board of directors may deem relevant. If we pay any dividends on our ordinary shares, we will pay those dividends which are payable in respect of the Class A ordinary shares underlying ADSs to the depositary, as the registered holder of such Class A ordinary shares, and the depositary will then pay such amounts to ADS holders in proportion to the Class A ordinary shares underlying the ADSs held by such ADS holders, subject to the terms of the deposit agreement, including the fees and expenses payable thereunder. See “Item 12. Description of Securities Other Than Equity Securities—D. American Depository Shares.” Cash dividends on our ordinary shares, if any, will be paid in U.S. dollars.

B. Significant Changes

Except as disclosed elsewhere in this annual report, we have not experienced any significant changes since the date of our audited consolidated financial statements included in this annual report.

Item 9. The Offer and Listing

A. Offer and Listing Details

Our ADSs, each representing two Class A ordinary shares, have been listed on The Nasdaq Global Market under the symbol “YI” since September 12, 2018.

B. Plan of Distribution

Not applicable.

C. Markets

The ADSs have been listed on Nasdaq since September 12, 2018 under the symbol “YI.”

D. Selling Shareholders

Not applicable.

E. Dilution

Not applicable.

F. Expenses of the Issue

Not applicable.

Item 10. Additional Information

A. Share Capital

Not applicable.

B. Memorandum and Articles of Association

We are a Cayman Islands exempted company and our affairs are governed by our memorandum and articles of association and the Companies Act (As Revised) of the Cayman Islands, referred to as the Companies Act below, and the common law of the Cayman Islands. The following are summaries of material provisions of our twelfth amended and restated memorandum and articles of association, as well as the Companies Act insofar as they relate to the material terms of our ordinary shares.

Registered Office and Objects

Our registered office in the Cayman Islands is located at the offices of Vistra (Cayman) Limited, P.O. Box 31119, Grand Pavilion Hibiscus Way, 802 West Bay Road, Grand Cayman, KY1-1205, Cayman Islands. Our agent for service of process in the United States is Puglisi & Associates. The objects of our company are unrestricted and we have the full power and authority to carry out any object not prohibited by the law of the Cayman Islands.

Board of Directors

See “Item 6. Directors, Senior Management and Employees—C. Board Practices—Board of Directors.”

Ordinary Shares

General

Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of our Class A ordinary shares and Class B ordinary shares will have the same rights except for voting and conversion rights, as described below. All of our outstanding ordinary shares are fully paid and non-assessable. Certificates representing the ordinary shares are issued in registered form. Our ordinary shares are issued in registered form and are issued when registered in our register of members. Our shareholders who are non-residents of the Cayman Islands may freely hold and vote their ordinary shares. Our company will issue only non-negotiable shares, and will not issue bearer or negotiable shares.

Conversion

Each Class B ordinary share may be converted into one Class A ordinary share at any time at the option of the holder thereof, while Class A ordinary shares cannot be converted into Class B ordinary shares under any circumstances.

Upon any sale, transfer, assignment or disposition of any Class B ordinary share by our Founders (defined in our memorandum and articles of association to mean Dr. Gang Yu and Mr. Junling Liu) or Founder Affiliate (as defined in our memorandum and articles of association) to any person who is not a “Founder Affiliate,” or upon a change of ultimate beneficial ownership of any Class B ordinary share to any person who is not a Founder Affiliate, such Class B ordinary share shall be automatically and immediately converted into one Class A ordinary share. However, the creation of any pledge, charge, encumbrance or other third party right on any Class B ordinary share to secure a holder’s contractual or legal obligations shall not be deemed as a sale, transfer, assignment or disposition unless and until any such pledge, charge, encumbrance or other third party right is enforced and results in the third party holding legal title to the relevant Class B ordinary shares, in which case all the related Class B ordinary shares shall be automatically converted into the same number of Class A ordinary shares.

Furthermore, if at any time the Founders and the Founder Affiliates collectively own less than 5% of the total number of the issued and outstanding shares of our company, all of the issued and outstanding Class B ordinary shares shall be automatically converted into the same number of Class A ordinary shares.

Register of Members

Under Cayman Islands law, we must keep a register of members and there should be entered therein:

- the names and addresses of the members, a statement of the shares held by each member, and of the amount paid or agreed to be considered as paid, on the shares of each member;
- confirm the number and category of shares held by each member, and confirm whether each relevant category of shares held by a member carries voting rights under the articles of association of the company, and if so, whether such voting rights are conditional;
- the date on which the name of any person was entered on the register as a member; and
- the date on which any person ceased to be a member.

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Under Cayman Islands law, the register of members of our company is *prima facie* evidence of the matters set out therein (i.e., the register of members will raise a presumption of fact on the matters referred to above unless rebutted) and a member registered in the register of members is deemed as a matter of Cayman Islands law to have legal title to the shares as set against its name in the register of members. Once our register of members has been updated, the shareholders recorded in the register of members should be deemed to have legal title to the shares set against their name.

If the name of any person is incorrectly entered in or omitted from our register of members, or if there is any default or unnecessary delay in entering on the register the fact of any person having ceased to be a member of our company, the person or member aggrieved (or any member of our company or our company itself) may apply to the Cayman Islands Grand Court for an order that the register be rectified, and the Court may either refuse such application or it may, if satisfied of the justice of the case, make an order for the rectification of the register.

Dividends

The holders of our ordinary shares are entitled to such dividends as may be declared by our board of directors or shareholders in a general meeting (provided always that dividends may be declared and paid only out of funds legally available therefor, namely out of either profit or our share premium account, and provided further that a dividend may not be paid if this would result in our company being unable to pay its debts as they fall due in the ordinary course of business). Our shareholders may by ordinary resolution declare a dividend, but no dividend may exceed the amount recommended by our board of directors.

Voting Rights

Holders of ordinary shares have the right to receive notice of, attend, speak and vote at general meetings of our company. Holders of Class A ordinary shares and Class B ordinary shares shall, at all times, vote together as one class on all matters submitted to a vote by the members at any general meeting of our company. Each Class A ordinary share shall entitle the holder thereof to one vote on all matters subject to the vote at general meetings of our company, and each Class B ordinary share shall entitle the holder thereof to fifteen votes on all matters subject to the vote at general meetings of our company. Voting at any meeting of shareholders is by show of hands unless a poll is demanded. A poll may be demanded by the chairman of such meeting or any one shareholder present in person or by proxy.

Maples and Calder (Hong Kong) LLP, our counsel as to Cayman Islands law, has advised that such voting structure is in compliance with current Cayman Islands law as in general terms, a company and its shareholders are free to provide in the articles of association for such rights as they consider appropriate, subject to such rights not being contrary to any provision of the Companies Act and not inconsistent with common law. Maples and Calder (Hong Kong) LLP has confirmed that the inclusion in our memorandum and articles of association of provisions giving weighted voting rights to specific classes of shareholders generally or to specific classes of shareholders on specific resolutions is not prohibited by the Companies Act. Further, weighted voting provisions have been held to be valid as a matter of English common law and therefore it is expected that such would be upheld by a Cayman Islands court.

An ordinary resolution to be passed by the shareholders requires the affirmative vote of a simple majority of the votes attached to the ordinary shares cast by those shareholders who are present in person or by proxy at a general meeting, while a special resolution requires the affirmative vote of no less than two-thirds of the votes attached to the ordinary shares cast by those shareholders who are present in person or by proxy at a general meeting. Both ordinary resolutions and special resolutions may also be passed by a unanimous written resolution signed by all the shareholders of our company, as permitted by the Companies Act and our memorandum and articles of association. A special resolution will be required for important matters such as a change of name or making changes to our memorandum and articles of association.

Transfer of Ordinary Shares

Any of our shareholders may transfer all or any of his or her ordinary shares by an instrument of transfer in the usual or common form or any other form approved by our board of directors. However, our board of directors may, in its absolute discretion, decline to

register any transfer of any ordinary share which is not fully paid up or on which our company has a lien. Our board of directors may also decline to register any transfer of any ordinary share unless:

- the instrument of transfer is lodged with us, accompanied by the certificate for the ordinary shares to which it relates and such other evidence as our board of directors may reasonably require to show the right of the transferor to make the transfer;
- the instrument of transfer is in respect of only one class of shares;
- the instrument of transfer is properly stamped, if required;
- any fee related to the transfer has been paid to us; and
- in the case of a transfer to joint holders, the transfer is not to more than four joint holders.

If our directors refuse to register a transfer, they are required, within three calendar months after the date on which the instrument of transfer was lodged, to send to each of the transferor and the transferee notice of such refusal. The registration of transfers of shares may, on ten calendar days' notice being given by advertisement in such one or more newspapers, by electronic means or by any other means in accordance with the relevant code, rules and regulations of the Nasdaq Global Market, be suspended and the register of members closed at such times and for such periods (not exceeding thirty calendar days in any calendar year) as our directors may determine.

Liquidation

On a return of capital on winding up or otherwise (other than on conversion, redemption or purchase of ordinary shares), assets available for distribution among the holders of ordinary shares will be distributed among the holders of the ordinary shares on a pro rata basis. If our assets available for distribution are insufficient to repay all of the paid-up capital, the assets will be distributed so that the losses are borne by our shareholders proportionately. We are a "limited liability" company registered under the Companies Act, and under the Companies Act, the liability of our members is limited to the amount, if any, unpaid on the shares respectively held by them. Our memorandum and articles of association contains a declaration that the liability of our members is so limited.

Calls on Ordinary Shares and Forfeiture of Ordinary Shares

Our board of directors may from time to time make calls upon shareholders for any amounts unpaid on their ordinary shares. The ordinary shares that have been called upon and remain unpaid are subject to forfeiture.

Redemption, Repurchase and Surrender of Ordinary Shares

We may issue shares on terms that such shares are subject to redemption, at our option or at the option of the holders thereof, on such terms and in such manner as may be determined, before the issue of such shares, by our board of directors or by a special resolution of our shareholders. Our company may also repurchase any of our shares provided that the manner and terms of such purchase have been approved by our board of directors or by an ordinary resolution of our shareholders or are otherwise authorized by our memorandum and articles of association. Under the Companies Act, the redemption or repurchase of any share may be paid out of our company's profits or out of the proceeds of a fresh issue of shares made for the purpose of such redemption or repurchase, or out of capital (including share premium account and capital redemption reserve) if our company can, immediately following such payment, pay its debts as they fall due in the ordinary course of business. In addition, under the Companies Act no such share may be redeemed or repurchased (a) unless it is fully paid up, (b) if such redemption or repurchase would result in there being no shares outstanding, or (c) if the company has commenced liquidation. In addition, our company may accept the surrender of any fully paid share for no consideration.

Variations of Rights of Shares

If at any time, our share capital is divided into different classes of shares, all or any of the rights attached to any class of shares may, subject to any rights or restrictions for the time being attached to any class, only be materially adversely varied with the consent in writing of the holders of two-thirds of the issued shares of that class or with the sanction of a special resolution passed at a separate meeting of the holders of shares of that class. The rights conferred upon the holders of the shares of any class issued with preferred or

other rights will not, subject to any rights or restrictions for the time being attached to the shares of that class, be deemed to be materially adversely varied by, inter alia, the creation, allotment or issue of further shares ranking pari passu with or subsequent to them or the redemption or purchase of any shares of any class by our company. The rights of the holders of shares shall not be deemed to be materially adversely varied by the creation or issue of shares with preferred or other rights including, without limitation, the creation of shares with enhanced or weighted voting rights.

General Meetings of Shareholders and Shareholder Proposals

As a Cayman Islands exempted company, we are not obliged by the Companies Act to call shareholders' annual general meetings.

Shareholders' annual general meetings and any other general meetings of our shareholders may be convened by the chairman of our board of directors, or any co-chairman of our board of directors, or by a majority of our board of directors. Advance notice of at least ten calendar days is required for the convening of our annual general shareholders' meeting and any other general meeting of our shareholders. A quorum required for a general meeting of shareholders consists of one or more shareholders present in person or by proxy (or, if a corporation or other non-natural person, by its duly authorized representative), holding shares which carry in aggregate not less than one-third of the total number of votes attaching to all issued and outstanding shares in our company which are entitled to vote at the meeting.

Cayman Islands law provides shareholders with only limited rights to requisition a general meeting, and does not provide shareholders with any right to put any proposal before a general meeting. However, these rights may be provided in a company's articles of association. Our memorandum and articles of association allow any shareholders holding shares which carry in aggregate not less than one-third of the total number of votes attaching to all issued and outstanding shares in our company, that carry the right to vote at general meetings of our company to requisition an extraordinary general meeting of our shareholders, in which case our directors are obliged to call such meeting and to put the resolutions so requisitioned to a vote at such meeting; however, our memorandum and articles of association do not provide our shareholders with any right to put any proposals before annual general meetings or extraordinary general meetings not called by such shareholders.

Election and Removal of Directors

Our memorandum and articles of association provide that, unless otherwise determined by our company in general meeting, our board will consist of not less than three directors. There are no provisions relating to retirement of directors upon reaching any age limit. Our board of directors may, by the affirmative vote of a simple majority of the remaining directors present and voting at a meeting of our board, which shall include the affirmative vote of at least one Founder as long as either Founder is a director, appoint any person as a director, to fill a vacancy on the board arising from the office of any director being vacated. In the event of a vacancy arising from the office of an independent director being vacated, our board may only appoint another independent director to fill such vacancy.

Our shareholders may also appoint any person to be a director by way of ordinary resolution. A director may be removed with or without cause by ordinary resolution. A vacancy on the board created by the removal of a director by ordinary resolution of our shareholders may be filled by an ordinary resolution or by the affirmative vote of a simple majority of the remaining directors present and voting at a meeting of our board. The notice of any meeting at which a resolution to remove a director shall be proposed or voted upon must contain a statement of the intention to remove that director and such notice must be served on that director not less than ten calendar days before the meeting. Such director is entitled to attend the meeting and be heard on the motion for his removal. In addition, a director will cease to be a director if, among other things, the director (i) becomes bankrupt or makes any arrangement or composition with his creditors, (ii) dies or is found by our company to be or becomes of unsound mind, (iii) resigns his office by notice in writing to the company, or (iv) without special leave of absence from our board, is absent from three consecutive board meetings and our directors resolve that his office be vacated.

Chairman and Co-chairmen of our Board

For so long as each of our founders is a director of our company, he shall be a co-chairman of our board of directors, until he resigns as co-chairman or ceases to be a director (in which event he shall automatically cease to be a co-chairman). If either founder ceases to be a co-chairman, the other founder shall continue as the sole chairman of our board (unless our board, with the consent of the other founder, elects and appoints another director to be another co-chairman). Upon both founders ceasing to be co-chairmen or chairman, our board shall elect and appoint the chairman or co-chairmen at their discretion.

Proceedings of Board of Directors

Our memorandum and articles of association provide that our business is to be managed and conducted by our board of directors. The quorum necessary for board meetings may be fixed by the board and, unless so fixed at another number, will be a majority of the directors. Our memorandum and articles of association provide that the board may from time to time at its discretion exercise all powers of our company to raise or borrow money, to mortgage or charge all or any part of the undertaking, property and assets (present and future) and uncalled capital of our company and issue debentures, bonds and other securities of our company, whether outright or as collateral security for any debt, liability or obligation of our company or of any third party.

Inspection of Books and Records

Holders of our ordinary shares have no general right under Cayman Islands law to inspect or obtain copies of our list of shareholders or our corporate records (other than copies of our memorandum and articles of association, our register of mortgages and charges, and any special resolutions passed by our shareholders). However, we intend to provide our shareholders with annual audited financial statements.

Changes in Capital

Our shareholders may from time to time by ordinary resolution:

- increase our share capital by such sum, to be divided into shares of such amount, as the resolution shall prescribe;
- consolidate and divide all or any of our share capital into shares of a larger amount than our existing shares;
- sub-divide our existing shares, or any of them into shares of a smaller amount than that fixed by our memorandum of association; or
- cancel any shares which, at the date of the passing of the resolution, have not been taken or agreed to be taken by any person and diminish the amount of our share capital by the amount of the shares so cancelled.

Our shareholders may by special resolution, subject to confirmation by the Grand Court of the Cayman Islands on an application by our company for an order confirming such reduction, reduce our share capital or any capital redemption reserve in any manner permitted by law.

Exempted Company

We are an exempted company incorporated with limited liability under the Companies Act. The Companies Act distinguishes between ordinary resident companies and exempted companies. Any company that is registered in the Cayman Islands but conducts business mainly outside of the Cayman Islands may apply to be registered as an exempted company. The requirements for an exempted company are essentially the same as for an ordinary company except for the exemptions and privileges listed below:

- an exempted company does not have to file an annual return of its shareholders with the Registrar of Companies of the Cayman Islands;
- an exempted company's register of members is not required to be open to inspection;
- an exempted company does not have to hold an annual general meeting;
- an exempted company may issue no par value, negotiable or bearer shares;
- an exempted company may obtain an undertaking against the imposition of any future taxation (such undertakings are usually given for 20 years in the first instance);
- an exempted company may register by way of continuation in another jurisdiction and be deregistered in the Cayman Islands;

- an exempted company may register as a limited duration company; and
- an exempted company may register as a segregated portfolio company.

“Limited liability” means that the liability of each shareholder is limited to the amount unpaid by the shareholder on that shareholder’s shares of the company (except in exceptional circumstances, such as involving fraud, the establishment of an agency relationship or an illegal or improper purpose or other circumstances in which a court may be prepared to pierce or lift the corporate veil).

We are subject to reporting and other informational requirements of the Exchange Act, as applicable to foreign private issuers. Except as otherwise disclosed in this annual report, we currently comply with the Nasdaq Global Market rules in lieu of following home country practice.

Differences in Corporate Law

The Companies Act is derived, to a large extent, from the older Companies Acts of England but does not follow recent United Kingdom statutory enactments, and accordingly there are significant differences between the Companies Act and the current Companies Act of England. In addition, the Companies Act differs from laws applicable to United States corporations and their shareholders. Set forth below is a summary of certain significant differences between the provisions of the Companies Act applicable to us and the laws applicable to companies incorporated in the United States and their shareholders.

Mergers and Similar Arrangements

The Companies Act permits mergers and consolidations between Cayman Islands companies and between Cayman Islands companies and non-Cayman Islands companies. For these purposes, (a) “merger” means the merging of two or more constituent companies and the vesting of their undertaking, property and liabilities in one of such companies as the surviving company and (b) a “consolidation” means the combination of two or more constituent companies into a combined company and the vesting of the undertaking, property and liabilities of such companies to the consolidated company. In order to effect such a merger or consolidation, the directors of each constituent company must approve a written plan of merger or consolidation, which must then be authorized by (a) a special resolution of the shareholders of each constituent company, and (b) such other authorization, if any, as may be specified in such constituent company’s articles of association. The written plan of merger or consolidation must be filed with the Registrar of Companies of the Cayman Islands together with a declaration as to the solvency of the consolidated or surviving company, a list of the assets and liabilities of each constituent company and an undertaking that a copy of the certificate of merger or consolidation will be given to the members and creditors of each constituent company and that notification of the merger or consolidation will be published in the Cayman Islands Gazette. Court approval is not required for a merger or consolidation which is effected in compliance with these statutory procedures.

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

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

Except in certain limited circumstances, a shareholder of a Cayman Islands constituent company who dissents from the merger or consolidation is entitled to payment of the fair value of his or her shares (which, if not agreed between the parties, will be determined by the Cayman Islands court) upon dissenting from a merger or consolidation, provided the dissenting shareholder complies strictly with the procedures set out in the Companies Act. The exercise of such dissenter rights will preclude the exercise by the dissenting shareholder of any other rights to which he or she might otherwise be entitled by virtue of holding shares, except for the right to seek relief on the grounds that the merger or consolidation is void or unlawful.

Separate from the statutory provisions relating to mergers and consolidations, the Companies Act also contains statutory provisions that facilitate the reconstruction and amalgamation of companies by way of schemes of arrangement, provided that the arrangement is approved by a majority in number of each class of shareholders or creditors with whom the arrangement is to be made and who must, in addition, represent three-fourths in value of each such class of shareholders or creditors, as the case may be, that are present and voting either in person or by proxy at a meeting, or meetings, convened for that purpose. The convening of the meetings and subsequently the arrangement must be sanctioned by the Grand Court of the Cayman Islands. While a dissenting shareholder has the right to express to the court the view that the transaction ought not to be approved, the court can be expected to approve the arrangement if it determines that:

- the statutory provisions as to the required majority vote have been met;
- the shareholders have been fairly represented at the meeting in question and the statutory majority are acting bona fide without coercion of the minority to promote interests adverse to those of the class;
- the arrangement is such that may be reasonably approved by an intelligent and honest man of that class acting in respect of his interest; and
- the arrangement is not one that would more properly be sanctioned under some other provision of the Companies Act.

The Companies Act also contains a statutory power of compulsory acquisition which may facilitate the “squeeze out” of dissentient minority shareholders upon a tender offer. When a tender offer is made and accepted by holders of 90% of the shares affected within four months, the offeror may, within a two-month period commencing on the expiration of such four month period, require the holders of the remaining shares to transfer such shares to the offeror on the terms of the offer. An objection can be made to the Grand Court of the Cayman Islands but this is unlikely to succeed in the case of an offer which has been so approved unless there is evidence of fraud, bad faith or collusion.

If an arrangement and reconstruction by way of scheme of arrangement is thus approved and sanctioned, or if a tender offer is made and accepted, in accordance with the foregoing statutory procedures, a dissenting shareholder would have no rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of Delaware corporations, providing rights to receive payment in cash for the judicially determined value of the shares.

Shareholders’ Suits

In principle, we will normally be the proper plaintiff to sue for a wrong done to us as a company, and as a general rule a derivative action may not be brought by a minority shareholder. However, based on English authorities, which would in all likelihood be of persuasive authority in the Cayman Islands, the Cayman Islands court can be expected to apply and follow the common law principles (namely the rule in *Foss v. Harbottle* and the exceptions thereto) which permit a minority shareholder to commence a class action against, or derivative actions in the name of, a company to challenge the following:

- an act which is illegal or ultra vires;
- an act which, although not ultra vires, could only be effected duly if authorized by a special or qualified majority vote that has not been obtained; and
- an act which constitutes a fraud on the minority where the wrongdoers are themselves in control of the company.

Indemnification of Directors and Executive Officers and Limitation of Liability

Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy, such as to provide indemnification against civil fraud or the consequences of committing a crime. Our memorandum and articles of association provide that we shall indemnify our directors and officers against all actions, proceedings, costs, charges, expenses, losses, damages or liabilities incurred or sustained by such director or officer, other than by reason of such person's own dishonesty, willful default or fraud, in or about the conduct of our company's business or affairs or in the execution or discharge of his duties, powers, authorities or discretions, including without prejudice to the generality of the foregoing, any costs, expenses, losses or liabilities incurred by such director or officer in defending (whether successfully or otherwise) any civil proceedings concerning our company or its affairs in any court whether in the Cayman Islands or elsewhere. This standard of conduct is generally the same as permitted under the Delaware General Corporation Law for a Delaware corporation. In addition, we have entered into indemnification agreements with our directors and senior executive officers that will provide such persons with additional indemnification beyond that provided in our memorandum and articles of association.

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

Anti-Takeover Provisions in the Memorandum and Articles of Association

Some provisions of our memorandum and articles of association may discourage, delay or prevent a change in control of our company or management that shareholders may consider favorable, including provisions that authorize our board of directors to issue preferred shares in one or more series and to designate the price, rights, preferences, privileges and restrictions of such preferred shares without any further vote or action by our shareholders.

However, under Cayman Islands law, our directors may only exercise the rights and powers granted to them under our memorandum and articles of association, as amended and restated from time to time, for a proper purpose and for what they believe in good faith to be in the best interests of our company.

Directors' Fiduciary Duties

Under Delaware corporate law, a director of a Delaware corporation has a fiduciary duty to the corporation and its shareholders. This duty has two components: the duty of care and the duty of loyalty. The duty of care requires that a director act in good faith, with the care that an ordinarily prudent person would exercise under similar circumstances. Under this duty, a director must inform himself of and disclose to shareholders, all material information reasonably available regarding a significant transaction. The duty of loyalty requires that a director act in a manner he or she reasonably believes to be in the best interests of the corporation. He or she must not use his or her corporate position for personal gain or advantage. This duty prohibits self-dealing by a director and mandates that the best interests of the corporation and its shareholders take precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the shareholders generally. In general, actions of a director are presumed to have been made on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the corporation. However, this presumption may be rebutted by evidence of a breach of one of the fiduciary duties. Should such evidence be presented concerning a transaction by a director, a director must prove the procedural fairness of the transaction and that the transaction was of fair value to the corporation.

As a matter of Cayman Islands law, a director of a Cayman Islands company is in the position of a fiduciary with respect to the company and therefore he owes the following duties to the company—a duty to act in good faith in the best interests of the company, a duty not to make a personal profit based on his or her position as director (unless the company permits him to do so), a duty not to put himself in a position where the interests of the company conflict with his or her personal interest or his or her duty to a third party and a duty to exercise powers for the purpose for which such powers were intended. A director of a Cayman Islands company owes to the company a duty to act with skill and care. It was previously considered that a director need not exhibit in the performance of his or her duties a greater degree of skill than may reasonably be expected from a person of his or her knowledge and experience. However, English and Commonwealth courts have moved towards an objective standard with regard to the required skill and care and these authorities are likely to be followed in the Cayman Islands.

Shareholder Proposals

Under the Delaware General Corporation Law, a shareholder has the right to put any proposal before the annual meeting of shareholders, provided it complies with the notice provisions in the governing documents. The Delaware General Corporation Law does not provide shareholders an express right to put any proposal before the annual meeting of shareholders, but in keeping with common law, Delaware corporations generally afford shareholders an opportunity to make proposals and nominations provided that they comply with the notice provisions in the certificate of incorporation or bylaws. A special meeting may be called by the board of directors or any other person authorized to do so in the governing documents, but shareholders may be precluded from calling special meetings.

Cayman Islands law provides shareholders with only limited rights to requisition a general meeting, and does not provide shareholders with any right to put any proposal before a general meeting. However, these rights may be provided in a company's articles of association. Our memorandum and articles of association provide that, on the requisition of any shareholders holding shares which carry in aggregate not less than one-third of the total number of votes attaching to all issued and outstanding shares in our company that carry the right to vote at general meetings of our company, our board of directors shall convene an extraordinary general meeting and put the resolutions so requisitioned to a vote at such meeting. However, our memorandum and articles of association do not provide our shareholders with any right to put any proposals before annual general meetings or extraordinary general meetings not called by such shareholders. As an exempted Cayman Islands company, we are not obliged by law to call shareholders' annual general meetings.

Cumulative Voting

Under the Delaware General Corporation Law, cumulative voting for elections of directors is not permitted unless the corporation's certificate of incorporation specifically provides for it. Cumulative voting potentially facilitates the representation of minority shareholders on a board of directors since it permits the minority shareholder to cast all the votes to which the shareholder is entitled on a single director, which increases the shareholder's voting power with respect to electing such director. Cayman Islands law does not prohibit cumulative voting, but our articles of association do not provide for cumulative voting. As a result, our shareholders are not afforded any less protections or rights on this issue than shareholders of a Delaware corporation.

Removal of Directors

Under the Delaware General Corporation Law, a director of a corporation with a classified board may be removed only for cause with the approval of a majority of the outstanding shares entitled to vote, unless the certificate of incorporation provides otherwise. Under our memorandum and articles of association, any of our directors may be removed by ordinary resolution of our shareholders.

Transactions with Interested Shareholders

The Delaware General Corporation Law contains a business combination statute applicable to Delaware public corporations whereby, unless the corporation has specifically elected not to be governed by such statute by amendment to its certificate of incorporation or bylaws that is approved by its shareholders, it is prohibited from engaging in certain business combinations with an "interested shareholder" for three years following the date that such person becomes an interested shareholder. An interested shareholder generally is a person or a group who or which owns or owned 15% or more of the target's outstanding voting stock or who or which is an affiliate or associate of the corporation and owned 15% or more of the corporation's outstanding voting stock within the past three years. This has the effect of limiting the ability of a potential acquirer to make a two-tiered bid for the target in which all shareholders would not be treated equally. The statute does not apply if, among other things, prior to the date on which such shareholder becomes an interested shareholder, the board of directors approves either the business combination or the transaction which resulted in the person becoming an interested shareholder. This encourages any potential acquirer of a Delaware corporation to negotiate the terms of any acquisition transaction with the target's board of directors.

Cayman Islands law has no comparable statute. As a result, we cannot avail ourselves of the types of protections afforded by the Delaware business combination statute. However, although Cayman Islands law does not regulate transactions between a company and its significant shareholders, it does provide that such transactions must be entered into bona fide in the best interests of the company and for a proper corporate purpose and not with the effect of constituting a fraud on the minority shareholders.

Dissolution; Winding Up

Under the Delaware General Corporation Law, unless the board of directors approves the proposal to dissolve, dissolution must be approved by shareholders holding 100% of the total voting power of the corporation. Only if the dissolution is initiated by the board of directors may it be approved by a simple majority of the corporation's outstanding shares. Delaware law allows a Delaware corporation to include in its certificate of incorporation a supermajority voting requirement in connection with dissolutions initiated by the board. Under Cayman Islands law, a company may be wound up by either an order of the courts of the Cayman Islands or by a special resolution of its members or, if the company is unable to pay its debts as they fall due, by an ordinary resolution of its members. The court has authority to order winding up in a number of specified circumstances including where it is, in the opinion of the court, just and equitable to do so.

Variation of Rights of Shares

Under the Delaware General Corporation Law, a corporation may vary the rights of a class of shares with the approval of a majority of the outstanding shares of such class, unless the certificate of incorporation provides otherwise. Under our memorandum and articles of association, if our share capital is divided into more than one class of shares, the rights attached to any such class may, subject to any rights or restrictions for the time being attached to any class, only be materially adversely varied with the consent in writing of the holders of two-thirds of the issued shares of that class or with the sanction of a special resolution passed at a separate meeting of the holders of the shares of that class.

Amendment of Governing Documents

Under the Delaware General Corporation Law, a corporation's certificate of incorporation may be amended only if adopted and declared advisable by the board of directors and approved by a majority of the outstanding shares entitled to vote and the bylaws may be amended with the approval of a majority of the outstanding shares entitled to vote and may, if so provided in the certificate of incorporation, also be amended by the board of directors. Under the Companies Act, our memorandum and articles of association may only be amended by special resolution of our shareholders.

Rights of Non-Resident or Foreign Shareholders

There are no limitations imposed by our memorandum and articles of association on the rights of non-resident or foreign shareholders to hold or exercise voting rights on our shares. In addition, there are no provisions in our memorandum and articles of association governing the ownership threshold above which shareholder ownership must be disclosed.

Directors' Power to Issue Shares

Under our memorandum and articles of association, our board of directors is empowered to issue or allot shares or grant options and warrants with or without preferred, deferred, qualified or other special rights or restrictions.

C. Material Contracts

We have not entered into any material contracts other than in the ordinary course of business and other than those described in "Item 4. Information on the Company" or elsewhere in this annual report on Form 20-F.

D. Exchange Controls

See "Item 4. Information on the Company—B. Business Overview—Regulations—Regulations Relating to Foreign Exchange and Dividend Distributions."

E. Taxation

The following summary of material Cayman Islands, PRC and U.S. federal income tax consequences of an investment in ADSs or ordinary shares is based upon laws and relevant interpretations thereof in effect as of the date of this annual report, all of which are subject to change. This summary does not deal with all possible tax consequences relating to an investment in ADSs or ordinary shares, such as the tax consequences under state, local and other tax laws.

Cayman Islands Taxation

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to investors levied by the government of the Cayman Islands except for stamp duties which may be applicable on instruments executed in, or, after execution, brought within the jurisdiction of the Cayman Islands. The Cayman Islands is not party to any double tax treaties which are applicable to any payments made by our company. There are no exchange control regulations or currency restrictions in the Cayman Islands.

Payments of dividends and capital in respect of ordinary shares and ADSs will not be subject to taxation in the Cayman Islands and no withholding will be required on the payment of a dividend or capital to any holder of ordinary shares or ADSs, nor will gains derived from the disposal of ordinary shares or ADSs be subject to Cayman Islands income or corporation tax.

No stamp duty is payable in respect of the issue of our ordinary shares or on an instrument of transfer in respect of our ordinary shares.

People's Republic of China Taxation

Although we are incorporated in the Cayman Islands, we may be treated as a PRC resident enterprise for PRC tax purposes under the EIT Law. The EIT Law provides that an enterprise established outside the PRC but whose “de facto management body” is located in the PRC is treated as a PRC resident enterprise for PRC tax purposes. The implementing rules of the EIT Law merely define the location of the “de facto management body” as “organizational body which effectively manages and controls the production and business operation, personnel, accounting, properties and other aspects of operations of an enterprise.” Based on a review of the facts and circumstances, we do not believe that 111, Inc. or Yao Wang Corporation Limited should be considered a PRC resident enterprise for PRC tax purposes. However, there is limited guidance and implementation history of the EIT Law. If 111, Inc. were to be considered a PRC resident enterprise, then PRC income tax at a rate of 10% would generally be applicable to any gain realized on the transfer of our ADSs or ordinary shares by investors that are “non-resident enterprises” of the PRC and to any interest or dividends payable by us to such investors. See “Item 3. Key Information—D. Risk Factors—Risks Related to Doing Business in China—If we are classified as a PRC resident enterprise for PRC income tax purposes, such classification could result in unfavorable tax consequences to us and our non-PRC shareholders or ADS holders.”

Furthermore, pursuant to the EIT Law and its implementation rules, if a non-resident enterprise has not set up an organization or establishment in the PRC, or has set up an organization or establishment but the income derived has no actual connection with such organization or establishment, it will be subject to a withholding tax on its PRC-sourced income at a rate of 10%. On February 3, 2015, the STA issued the Announcement on Several Issues Concerning the Enterprise Income Tax on Indirect Property Transfers by Non-PRC Resident Enterprises, pursuant to which the indirect transfer of assets of an “establishment or place” situated in China, by a non-PRC resident enterprise through a disposition of equity interests in an offshore holding company may also be treated as a transfer of PRC taxable assets and, as a result, the gain derived from this indirect transfer by a non-PRC enterprise shareholder (other than the sale at public stock market of shares that purchased by an offshore enterprise in public stock market) may be subject to PRC enterprise income tax at a rate of 10%. Therefore, the deposition of ADSs or ordinary shares acquired not at public stock market by investors in private transaction may subject to withholding tax rate at a rate of 10%.

Material U.S. Federal Income Tax Considerations

The following are material U.S. federal income tax consequences to the U.S. Holders described below of owning and disposing of the ADSs or Class A ordinary shares, but this discussion does not purport to be a comprehensive description of all of the tax considerations that may be relevant to a particular person's decision to hold the ADSs or Class A ordinary shares.

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This discussion applies to a U.S. Holder that holds the ADSs or Class A ordinary shares as capital assets for U.S. federal income tax purposes (generally, property held for investment). It does not describe all of the tax consequences that may be relevant in light of a U.S. Holder's particular circumstances, including the alternative minimum tax, the Medicare contribution tax on net investment income and tax consequences applicable to U.S. Holders subject to special rules, such as:

- certain financial institutions;
- dealers or traders in securities that use a mark-to-market method of tax accounting;
- persons holding ADSs or ordinary shares as part of a straddle, integrated or similar transaction;
- persons whose functional currency for U.S. federal income tax purposes is not the U.S. dollar;
- entities classified as partnerships for U.S. federal income tax purposes and their partners;
- tax-exempt entities, "individual retirement accounts" or "Roth IRAs";
- insurance companies;
- certain U.S. expatriates;
- persons that own or are deemed to own ADSs or ordinary shares representing 10% or more of our voting power or value;
- persons holding ADSs or ordinary shares in connection with a trade or business outside the United States; or
- persons who acquired our ADSs or ordinary shares pursuant to the exercise of an employee stock option or otherwise as compensation.

If a partnership (or other entity that is classified as a partnership for U.S. federal income tax purposes) owns ADSs or ordinary shares, the U.S. federal income tax treatment of a partner will generally depend on the status of the partner and the activities of the partnership. Partnerships owning ADSs or ordinary shares and their partners should consult their tax advisers as to their particular U.S. federal income tax consequences of owning and disposing of ADSs or ordinary shares.

This discussion is based on the Internal Revenue Code of 1986, as amended, (the "Code"), administrative pronouncements, judicial decisions, final, temporary and proposed Treasury regulations, and the income tax treaty between the United States and the PRC, or the Treaty, all as of the date hereof, any of which is subject to change, possibly with retroactive effect.

As used herein, a "U.S. Holder" is a person that is eligible for the benefits of the Treaty, and is a person that for U.S. federal income tax purposes is beneficial owner of our ADSs or Class A ordinary shares that is:

- a citizen or individual resident of the United States;
- a corporation, or other entity taxable as a corporation, created or organized in or under the laws of the United States, any state therein or the District of Columbia; or
- an estate or trust the income of which is subject to U.S. federal income taxation regardless of its source.

Treasury regulations that apply to taxable years beginning on or after December 28, 2021 (the "Foreign Tax Credit Regulations") may in some circumstances prohibit a U.S. person from claiming a foreign tax credit with respect to certain non-U.S. taxes that are not creditable under applicable income tax treaties. Accordingly, U.S. investors that are not eligible for Treaty benefits should consult their tax advisers regarding the creditability or deductibility of any PRC taxes imposed on dividends on, or dispositions of, the ADSs or ordinary shares. This discussion does not apply to investors in this special situation.

In general, a U.S. Holder that owns ADSs will be treated as the owner of the underlying ordinary shares represented by those ADSs for U.S. federal income tax purposes. Accordingly, no gain or loss will be recognized if a U.S. Holder exchanges ADSs for the underlying ordinary shares represented by those ADSs.

This discussion does not address any U.S. federal taxes (such as estate or gift taxes) other than income taxes, nor does it address any state, local or non-U.S. considerations. U.S. Holders should consult their tax advisers concerning the U.S. federal, state, local and non-U.S. tax consequences of owning and disposing of ADSs or ordinary shares in their particular circumstances.

Taxation of Distributions

This discussion is subject to the discussion below under “—Passive Foreign Investment Company Rules.”

Distributions paid on the ADSs or ordinary shares, other than certain pro rata distributions of ADSs or ordinary shares, will be treated as dividends to the extent paid out of our current or accumulated earnings and profits, as determined under U.S. federal income tax principles. Because we do not maintain calculations of our earnings and profits under U.S. federal income tax principles, it is expected that distributions generally will be reported to U.S. Holders as dividends. Dividends will not be eligible for the dividends-received deduction generally available to U.S. corporations under the Code. Subject to applicable limitations, dividends paid to certain non-corporate U.S. Holders may be taxable at a favorable rate. Non-corporate U.S. Holders should consult their tax advisers regarding the availability of this favorable rate in their particular circumstances.

Dividends will be included in a U.S. Holder’s income on the date of the U.S. Holder’s, or in the case of ADSs, the depositary’s, receipt. The amount of any dividend income paid in foreign currency will be the U.S. dollar amount calculated by reference to the spot rate in effect on the date of actual or constructive receipt, regardless of whether the payment is in fact converted into U.S. dollars on such date. If the dividend is converted into U.S. dollars on the date of receipt, a U.S. Holder generally should not be required to recognize foreign currency gain or loss in respect of the amount received. A U.S. Holder may have foreign currency gain or loss if the dividend is converted into U.S. dollars after the date of receipt.

Dividends will be treated as foreign-source income and will constitute passive category income or in certain cases, general category income, for foreign tax credit purposes. As described in “—People’s Republic of China Taxation,” dividends paid by us may be subject to PRC withholding tax. For U.S. federal income tax purposes, the amount of the dividend income will include any amounts withheld in respect of PRC withholding tax. Subject to applicable limitations, which vary depending upon the U.S. Holder’s circumstances, PRC taxes withheld from dividend payments (at a rate not exceeding the applicable rate provided in the Treaty) generally will be creditable against a U.S. Holder’s U.S. federal income tax liability. The rules governing foreign tax credits are complex, and U.S. Holders should consult their tax advisers regarding the creditability of foreign taxes in their particular circumstances. In lieu of claiming a credit, a U.S. Holder may elect to deduct such PRC taxes in computing its taxable income, subject to applicable limitations. An election to deduct creditable foreign taxes instead of claiming foreign tax credits must apply to all creditable foreign taxes paid or accrued in the relevant taxable year.

Sale or Other Taxable Disposition of ADSs or Ordinary Shares

This discussion is subject to the discussion below under “—Passive Foreign Investment Company Rules.”

A U.S. Holder will generally recognize capital gain or loss on a sale or other taxable disposition of ADSs or ordinary shares in an amount equal to the difference between the amount realized on the sale or disposition and the U.S. Holder’s tax basis in the ADSs or ordinary shares disposed of, in each case as determined in U.S. dollars. The gain or loss will be long-term capital gain or loss if, at the time of the sale or disposition, the U.S. Holder has owned the ADSs or ordinary shares for more than one year. Long-term capital gains recognized by non-corporate U.S. Holders are subject to tax rates that are lower than those applicable to ordinary income. The deductibility of capital losses is subject to limitations.

As described in “—People’s Republic of China Taxation,” gains on the sale of ADSs or ordinary shares may be subject to PRC taxes. Under the Code, capital gains of U.S. persons are generally treated as U.S.-source income. However, a U.S. Holder may be able to elect to treat the gain as foreign-source income under the Treaty and claim foreign tax credit in respect to any PRC tax on dispositions. The Foreign Tax Credit Regulations generally preclude a U.S. Holder from claiming a foreign tax credit with respect to PRC income taxes on gains from dispositions of ADSs or ordinary shares if the U.S. Holder does not elect to apply the benefits of the Treaty. However, in that case it is possible that any PRC taxes on disposition gains may either be deductible or reduce the amount

realized on the disposition. The rules governing foreign tax credits and deductibility of foreign taxes are complex. U.S. Holders should consult their tax advisers regarding the consequences of the imposition of any PRC tax on disposition gains, including the Treaty's resourcing rule, any reporting requirements with respect to a Treaty-based return position and the creditability or deductibility of the PRC tax in their particular circumstances (including any applicable limitations).

Passive Foreign Investment Company Rules

In general, a non-U.S. corporation is a passive foreign investment company for U.S. federal income tax purposes, or PFIC, for any taxable year in which (i) 75% or more of its gross income consists of passive income; or (ii) 50% or more of the value of its assets (generally determined on an average quarterly basis) consists of assets that produce, or are held for the production of, passive income. For purposes of the above calculations, a non-U.S. corporation that owns (or is treated as owning for U.S. federal income tax purposes), directly or indirectly, at least 25% by value of the shares of another corporation is treated as if it held its proportionate share of the assets of the other corporation and received directly its proportionate share of the income of the other corporation. Passive income generally includes dividends, interest, rents, royalties and certain gains. Cash is generally a passive asset for these purposes. Goodwill (the value of which generally may be determined by reference to the excess of the sum of the corporation's market capitalization and liabilities over the value of its assets) is generally characterized as a non-passive or passive asset based on the nature of the income produced in the activity to which the goodwill is attributable.

Based on the composition of our income and assets and the estimated value of our assets, including goodwill, which is based on the price of our ADSs, we believe that we were not a PFIC for our taxable year ended on December 31, 2021. However, our PFIC status for any taxable year will depend on the composition of our income and assets and the value of our assets from time to time (which may be determined, in large part, by reference to the market price of the ADSs, which has been and may continue to be volatile). Therefore, the risk of us being or becoming a PFIC will increase if during any taxable year our ADS price declines significantly.

Moreover, it is not entirely clear how the contractual arrangements for 2021 between our subsidiary, our variable interest entities and the shareholders of our variable interest entities should be treated for purposes of the PFIC rules, and we may have been a PFIC if our variable interest entities were not treated as owned by us for these purposes. In addition, the extent to which our goodwill should be characterized as an active asset is not entirely clear. We also hold a substantial amount of cash. Accordingly, there can be no assurance that we will not be a PFIC for our 2022 or any future taxable year.

If we were a PFIC for any taxable year and any of our subsidiaries or other companies in which we own or are treated as owning equity interests were also a PFIC (any such entity, a "Lower-tier PFIC"), U.S. Holders would be deemed to own a proportionate amount (by value) of the shares of each Lower-tier PFIC and would be subject to U.S. federal income tax according to the rules described in the subsequent paragraphs on (i) certain distributions by a Lower-tier PFIC and (ii) dispositions of shares of Lower-tier PFICs, in each case as if the U.S. Holders held such shares directly, even though the U.S. Holders would not receive the proceeds of those distributions or dispositions.

In general, if we were a PFIC for any taxable year during which a U.S. Holder held ADSs or ordinary shares, gain recognized by such U.S. Holder on a sale or other disposition (including certain pledges) of its ADSs or ordinary shares would be allocated ratably over that U.S. Holder's holding period. The amounts allocated to the taxable year of the sale or disposition and to any year before we became a PFIC would be taxed as ordinary income. The amount allocated to each other taxable year would be subject to tax at the highest rate in effect for individuals or corporations, as appropriate, for that taxable year, and an interest charge would be imposed on the resulting tax liability for each such year. Furthermore, to the extent that distributions received by a U.S. Holder in any year on its ADSs or ordinary shares exceed 125% of the average of the annual distributions on the ADSs or ordinary shares received during the preceding three years or the U.S. Holder's holding period, whichever is shorter, such distributions would be subject to taxation in the same manner.

If we are a PFIC for any taxable year during which a U.S. Holder owns ADSs or ordinary shares, we will generally continue to be treated as a PFIC with respect to the U.S. Holder for all succeeding years during which the U.S. Holder owns the ADSs or ordinary shares, even if we cease to meet the threshold requirements for PFIC status. If we are a PFIC for any taxable year but cease to be PFIC for subsequent years, U.S. Holders should consult their tax advisers regarding the advisability of making a "deemed sale" election that would allow them to eliminate the continuing PFIC status under certain circumstances.

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Alternatively, if we were a PFIC and if the ADSs were “regularly traded” on a “qualified exchange,” a U.S. Holder of ADSs could make a mark-to-market election that would result in tax treatment different from the general tax treatment for PFICs described above. The ADSs would be treated as “regularly traded” for any calendar year in which more than a de minimis quantity of the ADSs were traded on a qualified exchange on at least 15 days during each calendar quarter. The Nasdaq, where the ADSs are listed, is a qualified exchange for this purpose. If a U.S. Holder made the mark-to-market election, the U.S. Holder generally would recognize as ordinary income any excess of the fair market value of the ADSs at the end of each taxable year over their adjusted tax basis, and would recognize an ordinary loss in respect of any excess of the adjusted tax basis of the ADSs over their fair market value at the end of the taxable year (but only to the extent of the net amount of income previously included as a result of the mark-to-market election). If a U.S. Holder made the election, the U.S. Holder’s tax basis in the ADSs will be adjusted to reflect the income or loss amounts recognized. Any gain recognized on the sale or other disposition of ADSs in a year in which we were a PFIC would be treated as ordinary income and any loss would be treated as an ordinary loss (but only to the extent of the net amount of income previously included as a result of the mark-to-market election, with any excess treated as capital loss). If a U.S. Holder made the mark-to-market election, distributions paid on ADSs would be treated as discussed under “—Taxation of Distributions” above (but subject to the discussion in the immediately subsequent paragraph). U.S. Holders will not be able to make a mark-to-market election with respect to our ordinary shares or Lower-tier PFICs, if any. U.S. Holders should consult their tax advisers regarding the availability and advisability of a mark-to-market election if we were a PFIC for any taxable year.

We do not intend to provide information necessary for U.S. Holders to make qualified electing fund elections, which if available could materially affect the tax consequences of the ownership and disposition of ADSs.

If we were a PFIC (or with respect to a particular U.S. Holder were treated as a PFIC) for a taxable year in which we paid a dividend or for the prior taxable year, the favorable tax rate described above with respect to dividends paid to certain non-corporate U.S. Holders would not apply.

If we were a PFIC for any taxable year during which a U.S. Holder owned any ADSs or ordinary shares, the U.S. Holder would generally be required to file annual reports with the Internal Revenue Service. U.S. Holders should consult their tax advisers regarding the determination of whether we are a PFIC for any taxable year and the potential application of the PFIC rules to their ownership of ADSs or ordinary shares.

Information Reporting and Backup Withholding

Payments of dividends and sales proceeds that are made within the United States or through certain U.S.-related intermediaries may be subject to information reporting and backup withholding, unless (i) the U.S. Holder is a corporation or other “exempt recipient” or (ii) in the case of backup withholding, the U.S. Holder provides a correct taxpayer identification number and certifies that it is not subject to backup withholding. Backup withholding is not an additional tax. The amount of any backup withholding from a payment to a U.S. Holder will be allowed as a credit against the U.S. Holder’s U.S. federal income tax liability and may entitle it to a refund, provided that the required information is timely furnished to the Internal Revenue Service.

Certain U.S. Holders who are individuals (or certain specified entities) may be required to report information relating to their ownership of ADSs or ordinary shares, unless the ADSs or ordinary shares are held in accounts at financial institutions (in which case the accounts may be reportable if maintained by non-U.S. financial institutions). U.S. Holders should consult their tax advisers regarding their reporting obligations with respect to the ADSs or ordinary shares.

F. Dividends and Paying Agents

Not applicable.

G. Statement by Experts

Not applicable.

H. Documents on Display

We are subject to periodic reporting and other informational requirements of the Exchange Act as applicable to foreign private issuers, and are required to file reports and other information with the SEC. Specifically, we are required to file annually an annual

report on Form 20-F within four months after the end of each fiscal year, which is December 31. All information filed with the SEC can be obtained over the internet at the SEC's website at www.sec.gov or inspected and copied at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. You can request copies of documents, upon payment of a duplicating fee, by writing to the SEC. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and officers, directors and principal shareholders are exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Exchange Act.

We will furnish the Bank of New York Mellon, the depositary of the ADSs, with our annual reports, which will include a review of operations and annual audited consolidated financial statements prepared in conformity with U.S. GAAP, and all notices of shareholders' meetings and other reports and communications that are made generally available to our shareholders. The depositary will make such notices, reports and communications available to holders of ADSs and, upon our request, will mail to all record holders of ADSs the information contained in any notice of a shareholders' meeting received by the depositary from us.

I. Subsidiary Information

Not applicable.

Item 11. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

Our exposure to interest rate risk primarily relates to the interest income generated by excess cash, which is mostly held in interest-bearing bank deposits and financial instruments. These interest-bearing bank deposits and financial instruments carry a degree of interest rate risk. We have not been exposed to material risks due to changes in interest rates, and we have not used any derivative financial instruments to manage our interest risk exposure. However, our future interest income may fall short of expectations due to changes in market interest rates.

Foreign Exchange Risk

All of our net revenues and substantially all of our expenses are denominated in Renminbi. Our exposure to foreign exchange risk primarily relates to cash and cash equivalent denominated in U.S. dollars. We do not believe that we currently have any significant direct foreign exchange risk and have not used any derivative financial instruments to hedge exposure to such risk. Although our exposure to foreign exchange risks should be limited in general, the value of your investment in our ADSs will be affected by the exchange rate between U.S. dollar and Renminbi because the value of our business is effectively denominated in Renminbi, while our ADSs will be traded in U.S. dollars.

The value of Renminbi against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in political and economic conditions and the foreign exchange policy adopted by the PRC government. On July 21, 2005, the PRC government changed its policy of pegging the value of the Renminbi to the U.S. dollar. Following the removal of the U.S. dollar peg, the Renminbi appreciated more than 20% against the U.S. dollar over the following three years. Between July 2008 and June 2010, this appreciation halted and the exchange rate between the Renminbi and the U.S. dollar remained within a narrow band. Since June 2010, the PRC government has allowed the Renminbi to appreciate slowly against the U.S. dollar again, and it has appreciated more than 10% since June 2010. On August 11, 2015, the People's Bank of China announced plans to improve the central parity rate of the Renminbi against the U.S. dollar by authorizing market-makers to provide parity to the China Foreign Exchange Trading Center operated by the People's Bank of China with reference to the interbank foreign exchange market closing rate of the previous day, the supply and demand for foreign currencies as well as changes in exchange rates of major international currencies. Effective from October 1, 2016, the International Monetary Fund added Renminbi to its Special Drawing Rights currency basket. Such change and additional future changes may increase volatility in the trading value of the Renminbi against foreign currencies. The PRC government may adopt further reforms of its exchange rate system, including making the Renminbi freely convertible in the future. Accordingly, it is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between Renminbi and the U.S. dollar in the future.

To the extent that we need to convert U.S. dollars into Renminbi for our operations, appreciation of Renminbi against the U.S. dollar would reduce the Renminbi amount we receive from the conversion. Conversely, if we decide to convert Renminbi into U.S.

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dollars for the purpose of making payments for dividends on our ordinary shares or ADSs, servicing our outstanding debt, or for other business purposes, appreciation of the U.S. dollar against the Renminbi would reduce the U.S. dollar amounts available to us.

As of December 31, 2021, we had Renminbi-denominated cash and cash equivalents of RMB605.6 million (US\$95.0 million). A 10% depreciation of Renminbi against the U.S. dollar based on the foreign exchange rate on December 31, 2021 would result in a decrease of US\$9.5 million in cash and cash equivalents. A 10% appreciation of Renminbi against the U.S. dollar based on the foreign exchange rate on December 31, 2021 would result in an increase of US\$9.5 million in cash and cash equivalents.

Item 12. Description of Securities Other Than Equity Securities

A. Debt Securities

Not applicable.

B. Warrants and Rights

Not applicable.

C. Other Securities

Not applicable.

D. American Depository Shares

Fees and Charges Our ADS Holders May Have to Pay

The Bank of New York Mellon, as depositary, will register and deliver American Depository shares, also referred to as ADSs. Each ADS will represent two ordinary shares (or a right to receive two ordinary shares) deposited with The Hong Kong and Shanghai Banking Corporation Limited, as custodian for the depositary in Hong Kong. Each ADS will also represent any other securities, cash or other property which may be held by the depositary. The deposited shares together with any other securities, cash or other property held by the depositary are referred to as the deposited securities. The depositary's office at which the ADSs will be administered is located at 240 Greenwich Street, New York, New York 10286.

Persons depositing or withdrawing shares or ADS holders must pay:	For:
\$5.00 (or less) per 100 ADSs (or portion of 100 ADSs)	Issuance of ADSs, including issuances resulting from a distribution of shares or rights or other property
\$0.05 (or less) per ADS	Cancellation of ADSs for the purpose of withdrawal, including if the deposit agreement terminates
A fee equivalent to the fee that would be payable if securities distributed to you had been shares and the shares had been deposited for issuance of ADSs	Any cash distribution to ADS holders
\$0.05 (or less) per ADS per calendar year	Distribution of securities distributed to holders of deposited securities (including rights) that are distributed by the depositary to ADS holders
Registration or transfer fees	Depository services
Expenses of the depositary	Cable and facsimile transmissions (when expressly provided in the deposit agreement)
Taxes and other governmental charges the depositary or the custodian has to pay on any ADSs or shares underlying ADSs, such as stock transfer taxes, stamp duty or withholding taxes	Converting foreign currency to U.S. dollars
As necessary	As necessary
Any charges incurred by the depositary or its agents for servicing the deposited securities	As necessary

Fees and Other Payments Made by the Depositary to Us

The depositary has agreed to reimburse us annually for our expenses incurred in connection with investor relationship programs and any other program related to our ADS facility and the travel expense of our key personnel in connection with such programs. The depositary has also agreed to provide additional payments to us based on the applicable performance indicators relating to our ADS facility. There are limits on the amount of expenses for which the depositary will reimburse us, but the amount of reimbursement available to us is not necessarily tied to the amount of fees the depositary collects from investors. In 2021, we received net amount of \$766,677.66 incurred in connection with our investor relations and ADR program-related activities from the depositary.

PART II

Item 13. Defaults, Dividend Arrearages and Delinquencies

None.

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

Material Modifications to the Rights of Security Holders

See “Item 10. Additional Information—B. Memorandum and Articles of Association—Ordinary Shares” for a description of the rights of securities holders, which remain unchanged.

Use of Proceeds

The following “Use of Proceeds” information relates to the registration statement on Form F-1, as amended (File Number: 333-226849) in relation to our initial public offering of 7,175,000 ADSs representing 14,350,000 of our Class A ordinary shares, and the underwriters’ partial exercise of their option to purchase from us 809,555 additional ADSs representing 1,619,110 Class A ordinary shares, at an initial offering price of \$14.00 per ADS. J.P. Morgan Securities LLC, Citigroup Global Markets Inc. and China International Capital Corporation Hong Kong Securities Limited are the representatives of the underwriters.

As a result of our initial public offering, we raised an aggregate of approximately US\$ 101.2 million in net proceeds, after deducting underwriting commissions and the offering expenses payable by us. For the period from September 12, 2018, the date that the F-1 Registration Statement was declared effective by the SEC, to the date of this annual report, we used US\$101.2 million of the net proceeds from our initial public offering for general corporate purposes.

We still intend to use the proceeds from our initial public offering, as disclosed in our registration statements on Form F-1, for (i) general corporate purposes, including investment in product development, sales and marketing activities, technology infrastructure, capital expenditures, improvement of corporate facilities and other general and administrative matters, and (ii) acquisition of, or investment in, technologies, solutions or business that complement our business .

Item 15. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our chief executive officer and our chief financial officer, we carried out an evaluation of the effectiveness of our disclosure controls and procedures, which is defined in Rules 13a-15(e) of the Exchange Act, as of December 31, 2021. Based upon that evaluation, our management, with the participation of our chief executive officer and chief financial officer, has concluded that, as of the end of the period covered by this annual report, our disclosure controls and procedures were effective in ensuring that the information required to be disclosed by us in this annual report is recorded, processed, summarized and reported to them for assessment, and required disclosure is made within the time period specified in the rules and forms of the SEC.

Management’s Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15 (f) under the Exchange Act. Our management, with the participation of our chief executive officer and our chief financial officer, evaluated the effectiveness of our internal control over financial reporting based on criteria established in the framework in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, our management has concluded that our internal control over financial reporting was effective as of December 31, 2021.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

Attestation Report of the Registered Public Accounting Firm

Deloitte Touche Tohmatsu Certified Public Accountants LLP has audited the effectiveness of our internal control over financial reporting as of December 31, 2021 as stated in its report, which appears on page F-4 of this annual report on Form 20-F.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the year ended December 31, 2021 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 16A. Audit Committee Financial Expert

Our board of directors has determined that Mr. Nee Chuan Teo, an independent director (under the standards set forth in Nasdaq Stock Market Rule 5605(c)(2) and Rule 10A-3 under the Exchange Act) and chairman of our audit committee, is an audit committee financial expert.

Item 16B. Code of Ethics

Our board of directors adopted a code of business conduct and ethics that applies to our directors, officers, employees and advisors in August 2018. We have posted a copy of our code of business conduct and ethics on our website at <http://ir.111.com.cn>.

Item 16C. Principal Accountant Fees and Services

The following table sets forth the aggregate fees by categories specified below in connection with certain professional services rendered by Deloitte Touche Tohmatsu Certified Public Accountants LLP (PCAOB ID No. 1113), our principal external auditors, for the periods indicated.

	For the year ended December 31,		
	2019	2020	2021
	(in thousands)		
Audit fees and audit-related fees ⁽¹⁾	US\$ 935	US\$ 1,733	US\$ 1,324

(1) "Audit fees and audit-related fees" means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal auditors for the audit or review of our annual or quarterly financial statements, audit-related fees include service relating to the audit of the financial statements of 1 Pharmacy Technology in connection with its proposed initial public offering on the STAR Market since 2020, service to support the planned issuance of convertible senior notes in 2020.

The policy of our audit committee or our board of directors is to pre-approve all audit and non-audit services provided by Deloitte Touche Tohmatsu Certified Public Accountants LLP, including audit services, tax services and other services as described above.

Item 16D. Exemptions from the Listing Standards for Audit Committees

Not applicable.

Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers

On September 7, 2021, our board of directors authorized a share repurchase program, under which we may purchase up to US\$10 million of our Class A ordinary shares in the form of ADSs over the next 12 months from September 7, 2021. The US\$10 million share repurchase program was publicly announced on September 7, 2021. The table below summarizes the repurchases we made in the periods indicated.

Month	Total Number of Ordinary Shares Purchased	Average Price Paid Per Ordinary Share (US\$)	Total Number of Ordinary Shares Purchased as Part of Share Repurchase Program	Approximate Dollar Value of Ordinary Shares that may yet be Purchased Under Share Purchase Program (US\$, in million)
September 2021	—	—	—	10.00
October 2021	92,000	5.69	92,000	9.48
November 2021	74,500	5.31	74,500	9.08
December 2021	—	—	—	9.08
January 2022	—	—	—	9.08
February 2022	—	—	—	9.08
March 2022	—	—	—	9.08
April 1 through August 15, 2020	—	—	—	9.08

Item 16F. Change in Registrant's Certifying Accountant

Not applicable.

Item 16G. Corporate Governance

As a Cayman Islands exempted company listed on NASDAQ, we are subject to the Nasdaq corporate governance listing standards. However, NASDAQ rules permit a foreign private issuer like us to follow the corporate governance practices of its home country. Certain corporate governance practices in the Cayman Islands, which is our home country, may differ significantly from the Nasdaq corporate governance listing standards. See "Item 3. Key Information—D. Risk Factors—Risks Related to the American Depository Shares—We are a foreign private issuer within the meaning of the rules under the Exchange Act, and as such we are exempt from certain provisions applicable to U.S. domestic public companies."

Maples and Calder (Hong Kong) LLP, our Cayman Islands counsel, has provided letters to the Nasdaq Stock Market certifying that under Cayman Islands law, i) we are not required to have a majority of our board of directors comprised of independent directors, ii) we are not required to have a compensation committee of at least two members, each of whom must be an independent director, iii) we are not required to have a nominations committee comprised solely of independent directors, and iv) we are not required to hold annual shareholders meetings every year. We followed and intend to continue to follow our home country practice in lieu of the requirements to i) have our board of directors comprised of a majority of independent directors under Nasdaq Rule 5605(a)(2); (ii) have a compensation committee of at least two members, each of whom must be an independent director under Nasdaq Rule 5605(d)(2), (iii) have a nominations committee comprised solely of independent directors under Nasdaq Rule 5605(e)(1), and (iv) hold an annual meeting of shareholders no later than one year after the end of a fiscal year under Nasdaq Rule 5620(a).

Other than the home country practices described above, we are not aware of any significant differences between our corporate governance practices and those followed by U.S. domestic companies under Nasdaq Stock Market Rules.

Item 16H. Mine Safety Disclosure

Not applicable.

Item 16I. Disclosure Regarding Foreign Jurisdictions that Prevent Inspections

Not applicable.

PART III

Item 17. Financial Statements

We have elected to provide financial statements pursuant to Item 18.

Item 18. Financial Statements

The consolidated financial statements of 111, Inc., its subsidiaries and its consolidated affiliated entities are included at the end of this annual report.

Item 19. Exhibits

Exhibit Number	Description of Document
1.1	Twelfth Amended and Restated Memorandum and Articles of Association of the Registrant (incorporated by reference to Exhibit 3.2 of our registration statement on Form F-1 (file no. 333-226849), as amended, initially filed with the Securities and Exchange Commission on August 15, 2018)
2.1	Registrant's Specimen American Depository Receipt (incorporated by reference to Exhibit 4.1 of our registration statement on Form F-1 (file no. 333-226849), as amended, initially filed with the Securities and Exchange Commission on August 15, 2018)
2.2	Registrant's Specimen Certificate for Class A Ordinary Shares (incorporated by reference to Exhibit 4.2 of our registration statement on Form F-1 (file no. 333-226849), as amended, initially filed with the Securities and Exchange Commission on August 15, 2018)
2.3	Deposit Agreement between the Registrant, the Bank of New York Mellon and all owner and holders from time to time of ADSs issued thereunder, dated September 12, 2018 (incorporated by reference to Exhibit 4.3 of our registration statement on Form S-8 (file no. 333-229313), as amended, initially filed with the Securities and Exchange Commission on January 22, 2019)
2.4	Description of Securities (incorporated by reference to Exhibit 2.4 of our Annual Report on Form 20-F (file no. 001-38639) filed with the Securities and Exchange Commission on April 16, 2020)
4.1	English translation of 2013 Share Incentive Policy of the Registrant (incorporated by reference to Exhibit 10.1 of our Registration Statement on Form F-1 (file no. 333-226849) filed with the Securities and Exchange Commission on August 15, 2018)
4.2	English translation of 2014 Share Incentive Policy of the Registrant (incorporated by reference to Exhibit 10.2 of our Registration Statement on Form F-1 (file no. 333-226849) filed with the Securities and Exchange Commission on August 15, 2018)
4.3	The 2016 Share Incentive Plan of the Registrant (incorporated by reference to Exhibit 10.3 of our Registration Statement on Form F-1 (file no. 333-226849) filed with the Securities and Exchange Commission on August 15, 2018)
4.4	The 2018 Share Incentive Plan of the Registrant (incorporated by reference to Exhibit 10.4 of our Registration Statement on Form F-1 (file no. 333-226849) filed with the Securities and Exchange Commission on August 15, 2018)
4.5	Form of Employment Agreement between the Registrant and its executive officers (incorporated by reference to Exhibit 10.5 of our registration statement on Form F-1 (file no. 333-226849), as amended, initially filed with the Securities and Exchange Commission on August 15, 2018)
4.6	Form of Indemnification Agreement between the Registrant and its directors and executive officers (incorporated by reference to Exhibit 10.6 of our registration statement on Form F-1 (file no. 333-226849), as amended, initially filed with the Securities and Exchange Commission on August 15, 2018)

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Exhibit Number	Description of Document
4.21	English translation of Property Lease Contract between Kunshan Fuchan Warehousing Services Co., Ltd. and Yao Fang Information Technology (Shanghai) Co., Ltd. dated February 5, 2016 (incorporated by reference to Exhibit 10.21 of our registration statement on Form F-1 (file no. 333-226849), as amended, initially filed with the Securities and Exchange Commission on August 15, 2018)
4.22	English translation of Property Lease/Pre-lease Contract between Shanghai Zhangjiang Hi-tech Park Development Co., Ltd. and Yao Fang Information Technology (Shanghai) Co., Ltd. dated November 28, 2017 (incorporated by reference to Exhibit 10.22 of our registration statement on Form F-1 (file no. 333-226849), as amended, initially filed with the Securities and Exchange Commission on August 15, 2018)
4.26	English translation of Capital Increase Agreement in respect of Yao Fang Information Technology (Shanghai) Co., Ltd. dated August 10, 2020 (incorporated by reference to Exhibit 4.26 of our Annual Report on Form 20-F (file no. 001-38639) filed with the Securities and Exchange Commission on April 30, 2021)
4.27	English translation of Supplementary Agreement of Capital Increase Agreement in respect of Yao Fang Information Technology (Shanghai) Co., Ltd. dated August 26, 2020 (incorporated by reference to Exhibit 4.27 of our Annual Report on Form 20-F (file no. 001-38639) filed with the Securities and Exchange Commission on April 30, 2021)
4.28	English translation of Capital Increase Agreement in respect of 1 Pharmacy Yao Fang Technology (Shanghai) Co., Ltd. dated December 14, 2020 (incorporated by reference to Exhibit 4.28 of our Annual Report on Form 20-F (file no. 001-38639) filed with the Securities and Exchange Commission on April 30, 2021)
8.1*	List of Principal Subsidiaries and Consolidated Affiliated Entities
11.1	Code of Business Conduct and Ethics (incorporated by reference to Exhibit 99.1 of our Registration Statement on Form F-1 (file no. 333-226849) filed with the Securities and Exchange Commission on August 15, 2018)
12.1*	Certification by Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
12.2*	Certification by Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
13.1**	Certification by Principal Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
13.2**	Certification by Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
15.1*	Consent of Maples and Calder (Hong Kong) LLP
15.2*	Consent of Deloitte Touche Tohmatsu Certified Public Accountants LLP
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document
104*	Cover Page Interactive Data File (embedded within the Inline XBRL document)

* Filed herewith

** Furnished herewith

SIGNATURES

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

111, Inc.

By: /s/ Junling Liu

Name:Junling Liu

Title: Chief Executive Officer and Co-Chairman of the Board

Date: April 29, 2022

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111, INC.

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REPORTS OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO SHAREHOLDERS AND THE BOARD OF DIRECTORS OF 111, INC.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of 111, Inc. and its subsidiaries (the “Company”), as of December 31, 2021 and 2020, the related consolidated statements of comprehensive loss, changes in shareholders’ equity (deficit), and cash flows for each of the three years in the period ended December 31, 2021 and the related notes and the financial statement schedule (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2021 and 2020, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2021, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (the “PCAOB”), the Company’s internal control over financial reporting as of December 31, 2021, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 29, 2022 expressed an unqualified opinion on the Company’s internal control over financial reporting.

Convenience Translation

Our audits also comprehended the translation of Renminbi amounts into United States dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 2(ai). Such United States dollar amounts are presented solely for the convenience of readers in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matter

The critical audit matter communicated below is a matter arising from the current-period audit of the financial statements that was communicated or required to be communicated to the audit committee and that (1) relates to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of the critical audit matter does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing a separate opinion on the critical audit matter or on the accounts or disclosures to which it relates.

Revenue Recognition— Refer to Note 14 to the financial statements

Critical Audit Matter Description

As described in Note 14, the Company generated approximately 99.2% of its revenue from sales of medicines, healthcare products and other wellness merchandise through its online platforms in year 2021. The Company recognizes revenues from product sales at the point in time when the delivery was completed and uses automated systems to process and record its revenue transactions.

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We identified occurrence of product revenue as a critical audit matter because there is inherent risk around the occurrence of revenue recorded by the Company's systems given the complexity and the significant volume of data processed by the systems.

How the Critical Audit Matter Was Addressed in the Audit

Our audit procedures related to product revenue recognition included the following, among others:

With the assistance of our IT specialists and data specialists:

- We tested the IT environment in which the revenue transactions are processed, including interface controls between different IT applications.
- We tested key automated controls over product revenue recognition.
- We performed tests on the data to ensure consistency between different operating systems, consistency between operating systems and third-party information including delivery information from logistic companies and cash flow information from banks and third party payment service providers, and consistency between operating systems and accounting system, to evaluate data accuracy and completeness.
- We analyzed product revenue transaction data by comparing data in different periods and identifying transactions with characteristics of audit interest for further testing to verify the reasonableness of the transaction and other tests of details.

/s/ Deloitte Touche Tohmatsu Certified Public Accountants LLP

Shanghai, China

April 29, 2022

We have served as the Company's auditor since 2018.

REPORTS OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO SHAREHOLDERS AND THE BOARD OF DIRECTORS OF 111, INC.

Opinion on Internal Control over Financial Reporting

We have audited the internal control over financial reporting of 111, Inc. and its subsidiaries (the “Company”) as of December 31, 2021 based on criteria established in *Internal Control — Integrated Framework (2013 framework)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2021, based on the COSO criteria established in *Internal Control — Integrated Framework (2013)* issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (the “PCAOB”), the financial statements as of and for the year ended December 31, 2021 of the Company and our report dated April 29, 2022 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the convenience translation of Renminbi amounts into United States dollar amounts.

Basis for Opinion

The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control over Financial Reporting

A company’s internal control over financial reporting 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. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of the inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of the effectiveness to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/Deloitte Touche Tohmatsu Certified Public Accountants LLP
Shanghai, China
April 29, 2022

111, INC.
CONSOLIDATED BALANCE SHEETS
(Amounts in thousands, except for share and per share data)

	Notes	As of December 31,		
		2020	2021	2021 USS (Note 2 (ai))
ASSETS				
Current assets:				
Cash and cash equivalents		1,189,620	661,390	103,787
Restricted cash		128,914	99,282	15,580
Short-term investments	3	300,167	182,556	28,647
Accounts receivable, net of allowance of RMB429 and RMB1,148 as of December 31, 2020 and 2021, respectively		163,094	404,469	63,470
Notes receivable	4	12,583	90,734	14,238
Inventories	5	766,529	1,121,107	175,926
Prepayments and other current assets	6	311,797	242,199	38,006
Total current assets		2,872,704	2,801,737	439,654
Property and equipment	7	43,439	80,254	12,594
Intangible assets		6,517	4,909	770
Long-term investments		140	3,000	471
Operating lease right-of-use assets	8	98,628	233,847	36,696
Other non-current assets		5,061	22,086	3,465
Total assets		<u>3,026,489</u>	<u>3,145,833</u>	<u>493,650</u>
LIABILITIES AND EQUITY				
Current liabilities including amounts of the consolidated VIE without recourse to the Company (Note 2(b)):				
Short-term borrowings	9	229,250	259,658	40,746
Accounts payable		1,073,352	1,347,352	211,429
Accrued expenses and other current liabilities	10	327,118	522,968	82,065
Total current liabilities		<u>1,629,720</u>	<u>2,129,978</u>	<u>334,240</u>
Long-term operating lease liabilities	8	62,388	165,614	25,988
Other non-current liabilities		3,736	1,537	241
Total liabilities		<u>1,695,844</u>	<u>2,297,129</u>	<u>360,469</u>
Commitments and contingencies (Note 21)				
MEZZANINE EQUITY				
Redeemable non-controlling interests	11	<u>924,245</u>	<u>1,000,849</u>	<u>157,055</u>
SHAREHOLDERS' EQUITY (DEFICIT)				
Ordinary shares Class A (\$0.00005 par value per share; 800,000,000 shares authorized; 96,588,106 issued; 93,353,402 and 94,148,486 outstanding as of December 31, 2020 and 2021, respectively)	13	30	31	5
Ordinary shares Class B (\$0.00005 par value per share; 72,000,000 shares authorized, 72,000,000 shares issued and outstanding as of December 31, 2020 and 2021)	13	25	25	4
Treasury shares (1,997,620 and 2,330,620 shares as of December 31 2020 and 2021, respectively)		(34,972)	(40,859)	(6,412)
Additional paid-in capital		2,669,279	2,817,789	442,173
Accumulated deficit		(2,339,868)	(3,009,678)	(472,284)
Accumulated other comprehensive income		62,911	59,371	9,317
Total shareholders' equity (deficit)		<u>357,405</u>	<u>(173,321)</u>	<u>(27,197)</u>
Non-controlling interests	12	<u>48,995</u>	<u>21,176</u>	<u>3,323</u>
Total equity (deficit)		<u>406,400</u>	<u>(152,145)</u>	<u>(23,874)</u>
Total liabilities, mezzanine equity and equity (deficit)		<u>3,026,489</u>	<u>3,145,833</u>	<u>493,650</u>

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

111, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Amounts in thousands, except for share and per share data)

	Notes	Year Ended December 31,			
		2019 RMB	2020 RMB	2021 RMB	2021 US\$ (Note 2 (ai))
Net revenues	14	3,952,053	8,203,157	12,425,902	1,949,895
Operating costs and expenses:					
Cost of products sold		(3,786,870)	(7,837,325)	(11,804,807)	(1,852,432)
Fulfillment expenses		(128,996)	(226,930)	(355,836)	(55,838)
Selling and marketing expenses		(340,562)	(399,610)	(513,146)	(80,524)
General and administrative expenses		(123,501)	(128,226)	(206,981)	(32,480)
Technology expenses		(61,902)	(92,080)	(189,284)	(29,703)
Other operating (expenses) income, net		(3,735)	7,703	2,012	316
Total operating costs and expenses		<u>(4,445,566)</u>	<u>(8,676,468)</u>	<u>(13,068,042)</u>	<u>(2,050,661)</u>
Loss from operations		(493,513)	(473,311)	(642,140)	(100,766)
Interest income		4,802	6,312	9,776	1,534
Interest expense		(3,622)	(8,817)	(5,488)	(861)
Foreign exchange (loss) gain		(10,328)	5,547	1,937	304
Other income, net		834	3,161	14,890	2,337
Loss before income taxes		(501,827)	(467,108)	(621,025)	(97,452)
Income tax expense	17	—	—	—	—
Net loss		(501,827)	(467,108)	(621,025)	(97,452)
Net loss attributable to non-controlling interest		2,221	—	27,819	4,365
Net loss attributable to redeemable non-controlling interest		—	10,575	56,766	8,908
Adjustment attributable to redeemable non-controlling interest		—	—	(133,370)	(20,929)
Net loss attributable to ordinary shareholders		<u>(499,606)</u>	<u>(456,533)</u>	<u>(669,810)</u>	<u>(105,108)</u>
Other comprehensive income (loss), net of tax of nil					
Unrealized gains of available-for-sale securities		7,335	1,137	8,312	1,304
Realized gains of available-for-sale securities		(9,635)	(970)	(7,801)	(1,224)
Foreign currency translation adjustments		11,668	(13,697)	(4,051)	(635)
Comprehensive loss		<u>(490,238)</u>	<u>(470,063)</u>	<u>(673,350)</u>	<u>(105,663)</u>
Loss per share:					
Basic and diluted	16	<u>(3.05)</u>	<u>(2.77)</u>	<u>(4.04)</u>	<u>(0.63)</u>
Weighted average number of shares used in computation of loss per share:					
Basic and diluted	16	<u>163,671,577</u>	<u>164,786,631</u>	<u>165,866,901</u>	<u>165,866,901</u>

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

111, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (DEFICIT)
(Amounts in thousands, except for share data)

	Ordinary Shares Class A		Ordinary Shares Class B		Treasury Shares		Additional Paid-in Capital RMB	Accumulated Deficit RMB	Other Comprehensive Income (Loss) RMB	Non- controlling Interests RMB	Total Equity (Deficit) RMB
	Outstanding Shares	Amount RMB	Outstanding Shares	Amount RMB	Shares	Amount RMB					
Balance at January 1, 2019	91,088,106	29	72,000,000	25	—	—	2,540,878	(1,383,729)	67,073	(512)	1,223,764
Share-based compensation	—	—	—	—	—	—	54,281	—	—	—	54,281
Issuance of ordinary shares upon the exercise of stock options and vesting of restricted share units	2,517,780	1	—	—	—	—	11,327	—	—	—	11,328
Repurchase of shares	(1,485,862)	—	—	—	1,485,862	(22,991)	—	—	—	—	(22,991)
Net loss	—	—	—	—	—	—	—	(499,606)	—	(2,221)	(501,827)
Unrealized gains of available-for-sale securities, net of tax	—	—	—	—	—	—	—	—	7,335	—	7,335
Reclassification of realized gains, net of tax	—	—	—	—	—	—	—	—	(9,635)	—	(9,635)
Foreign currency translation, net of tax	—	—	—	—	—	—	—	—	11,668	—	11,668
Balance at December 31, 2019	92,120,024	30	72,000,000	25	1,485,862	(22,991)	2,606,486	(1,883,335)	76,441	(2,733)	773,923
Share-based compensation	—	—	—	—	—	75,695	—	—	—	—	75,695
Issuance of ordinary shares upon the exercise of stock options and vesting of restricted share units	1,745,136	—	—	—	—	—	6,326	—	—	—	6,326
Repurchase of shares	(511,758)	—	—	—	511,758	(11,981)	—	—	—	—	(11,981)
Capital contribution from non-controlling shareholders (Note 12)	—	—	—	—	—	—	(19,228)	—	—	51,728	32,500
Net loss	—	—	—	—	—	—	—	(467,108)	—	—	(467,108)
Net loss attributable to redeemable non-controlling interest	—	—	—	—	—	—	10,575	—	—	—	10,575
Unrealized gains of available-for-sale securities, net of tax	—	—	—	—	—	—	—	—	1,137	—	1,137
Reclassification of realized gains, net of tax	—	—	—	—	—	—	—	—	(970)	—	(970)
Foreign currency translation, net of tax	—	—	—	—	—	—	—	—	(13,697)	—	(13,697)
Balance at December 31, 2020	93,353,402	30	72,000,000	25	1,997,620	(34,972)	2,669,279	(2,339,868)	62,911	48,995	406,400
Share-based compensation	—	—	—	—	—	145,593	—	—	—	—	145,593
Issuance of ordinary shares upon the exercise of stock options and vesting of restricted share units	1,128,084	1	—	—	—	—	2,917	—	—	—	2,918
Repurchase of shares	(333,000)	—	—	—	333,000	(5,887)	—	—	—	—	(5,887)
Net loss	—	—	—	—	—	—	—	(593,206)	—	(27,819)	(621,025)
Net loss attributable to redeemable non-controlling interest	—	—	—	—	—	—	56,766	—	—	—	56,766
Adjustment attributable to redeemable non-controlling interest	—	—	—	—	—	—	(133,370)	—	—	—	(133,370)
Unrealized gains of available-for-sale securities, net of tax	—	—	—	—	—	—	—	—	8,312	—	8,312
Reclassification of realized gains, net of tax	—	—	—	—	—	—	—	—	(7,801)	—	(7,801)
Foreign currency translation, net of tax	—	—	—	—	—	—	—	—	(4,051)	—	(4,051)
Balance at December 31, 2021	94,148,486	31	72,000,000	25	2,330,620	(40,859)	2,817,789	(3,009,678)	59,371	21,176	(152,145)

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

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111, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in thousands)

	Year Ended December 31,			
	2019 RMB	2020 RMB	2021 RMB	2021 US\$ (Note 2 (ai))
Operating activities:				
Net loss	(501,827)	(467,108)	(621,025)	(97,452)
Adjustments to reconcile net income to net cash used in operating activities:				
Share-based compensation	54,281	75,695	145,593	22,847
Depreciation and amortization	11,668	14,017	27,221	4,272
(Gain) loss on disposal of property and equipment	(5)	162	(52)	(8)
Inventory write-down	790	24,216	45,976	7,215
Credit losses	—	(645)	1,339	210
Impairment loss	11,000	—	—	—
Investment Income	(9,635)	(970)	(7,801)	(1,224)
Noncash lease expense	25,394	39,303	89,785	14,089
Exchange Gain	—	(5,547)	—	—
Changes in operating assets and liabilities:				
Accounts receivable	(36,678)	(98,276)	(242,395)	(38,037)
Notes receivable	(23,587)	11,004	(78,151)	(12,263)
Inventories	(276,225)	(304,474)	(400,554)	(62,856)
Prepayments and other current assets	(47,457)	(102,119)	69,279	10,871
Other non-current assets	367	(2,052)	(17,025)	(2,671)
Accounts payable	232,076	629,018	274,000	42,997
Accrued expenses and other current liabilities	74,376	111,284	120,923	18,975
Operating lease liabilities	(24,721)	(38,085)	(93,751)	(14,712)
Other non-current liabilities	(2,199)	(2,200)	(2,199)	(345)
Net cash used in operating activities	<u>(512,382)</u>	<u>(116,777)</u>	<u>(688,837)</u>	<u>(108,092)</u>
Investing activities:				
Purchases of property and equipment	(20,030)	(25,505)	(62,592)	(9,822)
Purchases of intangible assets	(4,580)	(289)	(100)	(16)
Purchase of long-term investments	—	—	(3,000)	(471)
Proceeds from sale of long-term investments	—	—	140	22
Purchase of short-term investments	(601,000)	(500,000)	(1,832,427)	(287,548)
Proceeds from sale or maturity of short-term investments	863,106	200,970	1,957,801	307,222
Proceeds from disposition of property and equipment	179	155	316	50
Net cash provided by (used in) investing activities	<u>237,675</u>	<u>(324,669)</u>	<u>60,138</u>	<u>9,437</u>
Financing activities:				
Net proceeds from issuance of ordinary shares upon the exercise of stock options and vesting of restricted share units	11,328	6,326	2,918	458
Payment for share repurchase	(22,991)	(11,981)	(5,887)	(924)
Contribution from redeemable non-controlling interest holders	—	934,820	—	—
Contribution from non-controlling interest holders	—	32,500	—	—
Proceeds from short-term bank borrowings	150,919	398,766	406,837	63,842
Repayment of short-term bank borrowings	(55,838)	(264,597)	(376,429)	(59,070)
Proceeds from other financing activities	25,569	—	61,900	9,713
Repayment for other financing activities	—	(25,427)	(15,000)	(2,354)
Net cash provided by financing activities	<u>108,987</u>	<u>1,070,407</u>	<u>74,339</u>	<u>11,665</u>
Effect of exchange rate changes on cash and cash equivalents, and restricted cash	9,702	(8,149)	(3,502)	(550)
Net (decrease) increase in cash and cash equivalents, and restricted cash	(156,018)	620,812	(557,862)	(87,540)
Cash and cash equivalents, and restricted cash at the beginning of the year	853,740	697,722	1,318,534	206,907
Cash and cash equivalents, and restricted cash at the end of the year	<u>697,722</u>	<u>1,318,534</u>	<u>760,672</u>	<u>119,367</u>
Supplemental disclosure of cash flow information:				
Interest paid	818	10,865	5,625	883
Income tax paid	—	—	—	—
Supplemental disclosures of non-cash investing and financing activities:				
Change in fair value of available-for-sale investments	7,335	1,137	8,312	1,304
Purchases of property and equipment included in payables	1,133	1,771	6,476	1,016
Adjustment attributable to redeemable non-controlling interest	—	—	(133,370)	(20,929)

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the statement of financial position that sum to the total of the same such amounts shown in the statement of cash flows:

Cash and cash equivalents	581,281	1,189,620	661,390	103,787
Restricted cash	116,441	128,914	99,282	15,580
Cash and cash equivalents, and restricted cash	<u>697,722</u>	<u>1,318,534</u>	<u>760,672</u>	<u>119,367</u>

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

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111, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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1. ORGANIZATION AND PRINCIPAL ACTIVITIES

111, Inc. (the “Company”), was incorporated under the laws of the Cayman Islands in May 2013. The Company, through its subsidiaries, variable interest entities (“VIEs”) and VIE’s subsidiaries (collectively, the “Group”), operates an integrated online and offline platform in the healthcare ecosystem in China, whereby the Group is principally engaged in the sales of medical and wellness products through online retail and wholesale pharmacies and offline retail pharmacies, as well as provision of certain value-added services, such as online consultation services and e-prescription services to consumers in the People’s Republic of China (the “PRC”).

As of December 31, 2021, the Group operates its business mainly through the following subsidiaries:

Name of subsidiaries	Date of incorporation/establishment	Place of incorporation/establishment	Percentage of shareholdings	Principal activities
Yao Wang Corporation Limited (“Yao Wang”)	June 4, 2013	Hong Kong	100%	Investment holding
1 Pharmacy Technology (Shanghai) Co., Ltd. (previously known as Yaofang Information Technology (Shanghai) Co., Ltd., “1 Pharmacy Technology”)	August 12, 2013	Shanghai	86%	Warehousing, logistics, research and development, and consulting
Guangdong Yihao Pharmacy Co., Ltd. (“Yihao Pharmacy”)	March 7, 2003	Guangdong	VIE	Warehousing, logistics and procurement
Guangdong Yihao Pharmaceutical Chain Co., Ltd. (“Yihao Pharmaceutical Chain”)	November 1, 2001	Guangdong	VIE	Retail
Shanghai Yaowang E-commerce Co., Ltd. (“Shanghai Yaowang”)	January 15, 2013	Shanghai	VIE	Electronic Commerce
Wuhan Central China Drug Trading Co., Ltd. (“Wuhan Huazhong”)	August 5, 2015	Wuhan	70%	Software development and information technology support
Chongqing Yihao Pharmacy Co., Ltd. (“Chongqing Yihao Pharmacy”)	May 18, 2018	Chongqing	1 Pharmacy Technology’s subsidiary 1 Pharmacy Technology’s subsidiary	Warehousing and logistics
Tianjin Yihao Pharmacy Co., Ltd. (“Tianjin Yihao Pharmacy”)	June 20, 2018	Tianjin	1 Pharmacy Technology’s subsidiary	Warehousing and logistics
Kunshan Yifang Pharmacy Co., Ltd. (“Kunshan Yifang Pharmacy”)	July 30, 2018	Kunshan	VIE’s subsidiary 1 Pharmacy Technology’s subsidiary	Warehousing and logistics
Hubei Yihao Pharmacy Co., Ltd (“Hubei Yihao Pharmacy”)	Aug 31, 2019	Wuhuan	1 Pharmacy Technology’s subsidiary	Warehousing and logistics
Fujian Yaofang Pharmacy Co.,Ltd (“Fujian Yaofang Pharmacy”)	Aug 13, 2019	Fuzhou	1 Pharmacy Technology’s subsidiary	Warehousing and logistics
Shanxi Yaofang Pharmacy Co., Ltd (“Shanxi Yaofang Pharmacy”)	Oct 15, 2020	Shanxi	1 Pharmacy Technology’s subsidiary	Warehousing and logistics
Liaoning Yaofang Pharmacy Co., Ltd (“Liaoning Yaofang Pharmacy”)	Nov 6, 2020	Liaoning	1 Pharmacy Technology’s subsidiary	Warehousing and logistics

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES

(a) Basis of presentation

The financial statements of the Group have been prepared in accordance with the accounting principles generally accepted in the United States of America (“US GAAP”).

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(b) Basis of consolidation

The financial statements include the financial statements of the Company, its subsidiaries, VIEs and VIE's subsidiaries for which the Company is the primary beneficiary. All intercompany transactions, balances and unrealized profit and losses have been eliminated upon consolidation.

The Group evaluates the need to consolidate certain variable interest entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support or the entity is structured with disproportionate voting rights, and substantially all of the activities are conducted on behalf of an investor with disproportionately few voting rights.

The Group is deemed as the primary beneficiary of and consolidates variable interest entities when the Group has the power to direct the activities that most significantly impact the economic success of the entities and effectively assumes the obligation to absorb losses or has the rights to receive benefits that are potentially significant to the entities.

As of the commence date of the Group, as a foreign-invested company engaged in Internet-based businesses, the Group is subject to significant restrictions under current PRC laws and regulations, specifically the Company and its PRC subsidiary, 1 Pharmacy Technology, are both restricted from holding the licenses that are necessary for the online operation in China. To comply with these restrictions, the Company conducts the online operations principally through Yihao Pharmacy. Yihao Pharmacy holds the licenses necessary to conduct the internet-related operations of 1 Medicine Marketplace and 1 Pharmacy in China.

Since the Company does not have any equity interests in Yihao Pharmacy, in order to exercise effective control over its operations, the Company, through its wholly owned subsidiary, 1 Pharmacy Technology, entered into a series of contractual arrangements with Yihao Pharmacy and its shareholders, pursuant to which the Company is entitled to receive effectively all economic benefits generated from Yihao Pharmacy shareholders' equity interests in it. Details of the key agreements entered into between 1 Pharmacy Technology, Yihao Pharmacy and each of its two individual shareholders nominated by the Founders ("Nominees") in September 2013 are as follows:

Exclusive Option Agreement: Under the exclusive option agreement, the Nominees granted an irrevocable assets and equity option to 1 Pharmacy Technology, that entitles 1 Pharmacy Technology or its designated entity or individual to acquire all or a portion of the assets owned by Yihao Pharmacy and its subsidiaries and all the equity interests held by nominees in Yihao Pharmacy and its subsidiaries at its sole discretion, at zero price or the lowest price permitted under PRC laws then in effect. The option may be exercised by 1 Pharmacy Technology or its designee. The exclusive option agreement remains effective for the same period as the exclusive support service agreement.

Proxy Agreement: Under the shareholder voting right proxy agreement, the Nominees irrevocably grant any person designated by 1 Pharmacy Technology the power to exercise all voting rights. This Agreement may not be terminated without the consent of 1 Pharmacy Technology, which may unilaterally terminate the agreement, by giving a thirty (30) day prior written notice to the Nominees. The proxy agreement remains in force for the same period as the exclusive support services agreement.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(b) Basis of consolidation (Continued)

The agreements that transfer economic benefits to the Company include:

Equity Pledge Agreement: Under the equity pledge agreement, all of the equity interest in Yihao Pharmacy were pledged to 1 Pharmacy Technology to guarantee the performance of the obligations of Yihao Pharmacy and Nominees under the exclusive support services agreement, the proxy agreement, the exclusive option agreement, and repayment of all accounts payable to 1 Pharmacy Technology from time to time. If the Nominees or Yihao Pharmacy breach their respective contractual obligations, 1 Pharmacy Technology, as pledgee, will be entitled to certain rights, including the right to dispose the pledged equity interests. Pursuant to the equity pledge agreement, the Nominees shall not transfer, assign or otherwise create any new encumbrance on their respective equity interest in Yihao Pharmacy without the prior written consent of 1 Pharmacy Technology. The equity pledge right enjoyed by 1 Pharmacy Technology will expire when the Nominees and Yihao Pharmacy have fully performed their respective contractual obligations, including but not limited to pay services fees to the 1 Pharmacy Technology under the exclusive support services agreement, authorize the 1 Pharmacy Technology to act as its attorney-in fact to exercise shareholders' rights of Nominees under the proxy agreements, grant exclusive option to the 1 Pharmacy Technology or any third party designated by 1 Pharmacy Technology to purchase all or part of their respective equity interests at the lowest price permitted by law under the exclusive option agreements, and repay all accounts payable to 1 Pharmacy Technology.

Exclusive Support Service Agreement: Pursuant to the exclusive support service agreement, 1 Pharmacy Technology provides Yihao Pharmacy with a series of technical support services and is entitled to receive related fees. This agreement shall be in full force and effective until Yihao Pharmacy's valid operation term as stated on business license expires. During the term of this agreement, 1 Pharmacy Technology shall be the exclusive provider of the services. Yihao Pharmacy shall not seek or accept similar services from other providers without the prior written approval of 1 Pharmacy Technology. The agreement will remain effective for ten years and will be automatically extended for another ten years thereafter, unless 1 Pharmacy Technology terminates the agreement or it is terminated in advance pursuant to other provisions of the agreement such as bankruptcy of one party or one party's failure to perform its obligation for more than six consecutive months due to a force majeure event.

In September 2019, exclusive support services agreements with each of the variable interest entities were amended, pursuant to which, the variable interest entities agree to pay service fees in an amount equivalent to the balance calculated as 3% of quarterly revenue (exclusive of revenue from related parties) of the variable interest entities on a quarterly basis. 1 Pharmacy Technology has the right to delay or waive payment of service fees at its discretion and the service fee level is subject to adjustment at any time upon mutual agreement between 1 Pharmacy Technology and the variable interest entities.

Similar contractual agreements were also entered into by 1 Pharmacy Technology, Yihao Pharmaceutical Chain and Yao Wang, and their respective shareholders in September 2013 and September 2019.

US GAAP provides guidance on the identification of VIE and financial reporting for entities over which control is achieved through means other than voting interests. The Group evaluates each of its interests in an entity to determine whether or not the investee is a VIE and, if so, whether the Group is the primary beneficiary of such VIE. In determining whether the Group is the primary beneficiary, the Group considers if the Group (1) has power to direct the activities that most significantly affect the economic performance of the VIE, and (2) receives the economic benefits of the VIE that could be significant to the VIE. If deemed the primary beneficiary, the Group consolidates the VIE.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(b) Basis of consolidation (Continued)

The irrevocable power of attorney has conveyed all shareholder rights held by the VIEs' shareholders to 1 Pharmacy Technology, including the right to appoint board members who nominate the general managers of the VIEs to conduct day-to-day management of the VIEs' businesses, and to approve significant transactions of the VIEs. In addition, the exclusive option agreements provide 1 Pharmacy Technology with a substantive kick-out right of the VIEs shareholders through an exclusive option to purchase all or any part of the shareholders' equity interest in the VIEs at zero price or the lowest price permitted under PRC laws then in effect. In addition, through the exclusive support services agreements, the Company established the right to receive benefits from the VIEs that could potentially be significant to the VIEs, and through the equity pledge agreement, the Company has, in substance, an obligation to absorb losses of the VIEs that could potentially be significant to the VIEs.

Risks in relation to the VIE structure

The Group believes that the VIE arrangements are in compliance with PRC law and are legally enforceable. However, there are certain risks related to the VIE arrangements, which include but are not limited to the following:

- If the Group's ownership structure is found to be in violation of any existing or future PRC laws or regulations, the relevant governmental authorities, including the China Securities Regulatory Commission, would have broad discretion in dealing with such violation, including levying fines, confiscating its income or the income of 1 Pharmacy Technology, revoking the business licenses or operating licenses of 1 Pharmacy Technology, shutting down the Group's servers or blocking the Group's websites, discontinuing or placing restrictions or onerous conditions on the Group's operations, requiring the Group to undergo a costly and disruptive restructuring, restricting or prohibiting the Group's use of various funding to finance its business and operations in China, and taking other regulatory or enforcement actions that could be harmful to the Group's business;
- The Group relies on contractual arrangements with the VIEs and their equity holders for a majority of its PRC operations, which may not be as effective as direct ownership in providing operational control;
- The Group may have to incur significant cost to enforce, or may not be able to effectively enforce, the contractual arrangements with the VIEs and their equity holders in the event of a breach or non-compliance by the VIEs or their equity holders;
- Under the contractual arrangements with the VIEs and their shareholders, (a) the Company may replace any such individual as a shareholder of the VIEs at the Company's discretion, and (b) each of two individuals has executed a power of attorney to appoint 1 Pharmacy Technology or its designated third party to vote on their behalf and exercise shareholder rights of the VIE. However, the Company cannot assure that these individuals will act in the best interests of the Company should any conflicts of interest arise, or that any conflicts of interest will be resolved in the Company's favor. These individuals may breach or cause the VIE to breach the existing contractual arrangements. If the Company cannot resolve any conflicts of interest or disputes between the Company and any of these individuals, the Company would have to rely on legal proceedings, which may be expensive, time-consuming and disruptive to its operations. There is also substantial uncertainty as to the outcome of any such legal proceedings.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(b) Basis of consolidation (Continued)

The following amounts and balances of the VIEs were included in the Group's financial statements after the elimination of intercompany balances and transactions:

	As of December 31,	
	2020	2021
Current Assets:		
Cash and cash equivalents	73,838	147,192
Restricted cash	57,638	107
Accounts receivable, net	143,210	180,901
Notes receivable, net	5,496	23,418
Inventories	298,020	397,993
Prepayments and other current assets	246,264	129,036
Total current assets	824,466	878,647
Property and equipment	10,168	23,793
Intangible assets, net	920	862
Long-term investments	140	—
Operating lease right-of-use assets	52,439	85,239
Other non-current assets	2,367	11,810
Total assets	890,500	1,000,351
 Current Liabilities:		
Accounts payable	(667,032)	(614,527)
Accrued expenses and other current liabilities	(58,975)	(146,570)
Total current liabilities	(726,007)	(761,097)
Long-term operating lease liabilities	(33,843)	(62,018)
Total liabilities	(759,850)	(823,115)

	Year Ended December 31,		
	2019	2020	2021
Net revenues	3,302,818	4,523,586	5,046,378
Total cost and expenses	(3,383,187)	(4,565,505)	(4,966,795)
Net (loss) income	(80,369)	(41,919)	79,583

	Year Ended December 31,		
	2019	2020	2021
Net cash used in operating activities	(263,750)	(194,149)	(151,421)
Net cash used in investing activities	(4,684)	(4,180)	(17,967)
Net cash provided by (used in) financing activities	87,892	(64,963)	13,355

The VIEs contributed approximately 84%, 55% and 41% of the Group's consolidated revenues for each of the years ended December 31, 2019, 2020 and 2021. As of December 31, 2020 and 2021, the VIEs accounted for an aggregate of approximately 29% and 32%, respectively, of the consolidated total assets, and approximately 45% and 36%, respectively, of the consolidated total liabilities.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(b) Basis of consolidation (Continued)

Since September 2013, 1 Pharmacy Technology started paying service fees to external suppliers for the VIEs and recharges all or portion of these expenses to the VIEs at cost given that VIEs are in a loss position. Since VIE contract amendment in September 2019, service fees were calculated as 3% of quarterly revenue (exclusive of revenue from related parties) of the variable interest entities. The service fees charged by 1 Pharmacy Technology to the VIEs were RMB 126,831, RMB 206,083 and RMB 257,623 for the years ended December 31, 2019, 2020 and 2021, respectively. There are no terms in any arrangements, considering both explicit arrangements and implicit variable interests that require the Company or its subsidiaries to provide financial support to the VIEs. However, if the VIEs ever need financial support, the Company or its subsidiaries may, at its option and subject to statutory limits and restrictions, provide financial support to its VIEs through loans to the shareholders of the VIEs or entrustment loans to the VIEs.

The Group believes that there are no assets held in the consolidated VIE that can be used only to settle obligations of the VIEs, except for registered capital and the PRC statutory reserves. As the consolidated VIEs are incorporated as limited liability companies under the PRC Company Law, creditors of the VIEs do not have recourse to the general credit of the Company for any of the liabilities of the consolidated VIE.

Relevant PRC laws and regulations restrict the VIEs from transferring a portion of their net assets, equivalent to the balance of their statutory reserve and their share capital, to the Company in the form of loans and advances or cash dividends.

(c) Use of estimates

The preparation of the financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the period. Areas where management uses subjective judgment include estimating inventory net realizable value and assumptions used in valuation of share-based compensation. Management bases the estimates on historical experience and various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results could differ from these estimates.

(d) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and demand deposits, which are unrestricted as to withdrawal and use, and which have original maturities of three months or less when purchased.

(e) Restricted cash

Restricted cash mainly represents the Group's deposits to the banks as a form of security with respect to the Group's debt. The cash held as deposits in the bank are not available to fund the general operating purposes of the Group.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(f) Short-term investments

Short-term investments include (i) structured deposits from commercial banks with guaranteed principal and variable interest rates indexed to the performance of underlying assets and with maturities within one year; (ii) fund products purchased from certain financial institutions with maturities within one year. The Group classifies the short-term investments in debt securities as held-to-maturity when it has both the positive intent and ability to hold them until maturity. Short-term investments that are bought and held principally for the purpose of selling them in the near term are classified as trading securities. Short-term investments that do not meet the criteria of held-to-maturity or trading securities are classified as available-for-sale, and are reported at fair value with changes in fair value with the unrealized gains or losses recorded in accumulated other comprehensive income (loss) as a component of shareholders' equity (deficit). The Group has no intent to hold the debt securities till maturity or may sell the debt securities in response to the changes in economic conditions and classified all short-term investments as available-for-sale debt securities as of December 31, 2020 and 2021.

Before the adoption of Accounting Standards Update ("ASU") 2016-13 the amount of the total impairment related to the credit loss was recognized in the income statement and the amount related to all other factors is recognized in other comprehensive income, net of applicable taxes, and the impairment losses recognized in the income statement cannot be reversed for any future recoveries. After the adoption of ASC 326 on January 1, 2020, credit-related impairment is measured as the difference between the debt security's amortized cost basis and the present value of expected cash flows and is recognized as an allowance on the balance sheet with a corresponding adjustment to earnings. The allowance should not exceed the amount by which the amortized cost basis exceeds fair value. As of December 31, 2020 and 2021, the fair value of the Group's available-for-sale debt securities is equal to their amortized cost amounting to RMB 300,167 and RMB 182,556, respectively. The Group did not identify any factors that are indicative of impairment with respect to its available-for-sale debt securities.

(g) Accounts receivable, net

Accounts receivable mainly consists of amounts due from the Group's customers, which is recorded net of allowance for credit losses.

Since January 1, 2020, the Group adopted ASU No. 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments using the modified retrospective transition method. The Group applied a current expected credit losses ("CECL") model for financial instruments measured at amortized cost. The Group has developed a CECL model based on historical experience, the age of the accounts receivable balances, credit quality of its customers, economic conditions, and other factors that may affect its ability to collect from customers.

	Total allowance for credit losses
Balance at December 31, 2019	—
Credit loss expense	429
Write-offs	—
Balance at December 31, 2020	429
Credit loss expense	1,020
Write-offs	(301)
Balance at December 31, 2021	1,148

111, INC.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED DECEMBER 31, 2019, 2020 and 2021****(Amounts in thousands, except for share data and per share data, unless otherwise stated)****2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)****(h) Inventories**

Inventories, consisting of products available for sale, are accounted for using the weighted average cost method, and are valued at lower of cost or the net realizable value. Adjustments are recorded to write down the cost of inventory to the estimated market value due to slow-moving or damaged products, which is dependent upon factors such as historical and forecasted consumer demand, and promotional environment. Write-downs are recorded in cost of products sold in the consolidated statements of comprehensive loss.

(i) Property and equipment

Property and equipment are stated at cost less accumulated depreciation and impairment. The renovations, betterments and interest cost incurred during construction are capitalized. Property and equipment are depreciated at their costs less impairment and residual value, if any, over the estimated useful lives on a straight-line basis. The estimated useful lives are as follows:

Leasehold improvements	Shorter of the lease term or their estimated useful lives
Furniture, fixtures and equipment	3-5 years
Electronic equipment	3-5 years
Vehicles	4-5 years

Construction in progress represents leasehold improvements under construction or being installed and is stated at cost. Cost comprises original cost of property and equipment, installation, construction and other direct costs. Construction in progress is transferred to leasehold improvements and depreciation commences when the asset is ready for its intended use.

Expenditures for repairs and maintenance are expensed as incurred. Gain or loss on disposal of property and equipment, if any, is recognized in the consolidated statements of comprehensive loss as the difference between the net sales proceeds and the carrying amount of the underlying asset. There was no interest cost capitalized during the years ended December 31, 2019, 2020 and 2021.

(j) Intangible assets

Intangible assets mainly consist of externally purchased software and licenses. Software are amortized over an estimated useful life of ten years on a straight-line basis. Licenses are amortized over the remaining estimated useful life on a straight-line basis.

(k) Impairment of long-lived assets

Long-lived assets are evaluated for impairment whenever events or changes in circumstances (such as a significant adverse change to market conditions that will impact the future use of the assets) indicate that the carrying value of an asset may not be fully recoverable. When these events occur, the Group evaluates the impairment for the long-lived assets by comparing the carrying value of the assets to an estimate of future undiscounted cash flows expected to be generated from the use of the assets and their eventual disposition. If the sum of the expected future undiscounted cash flows is less than the carrying value of the assets, the Group recognizes an impairment loss based on the excess of the carrying value of the assets over the fair value of the assets. For the years ended December 31, 2019, 2020 and 2021, there was no impairment recognized for the Group's long-lived assets.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(l) Long-term investments

The Group's investments in equity investees consist of investments in equity securities without readily determinable fair values and equity method investments in privately-held companies.

The Group measures its equity securities without a readily determinable fair value at its cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer.

The Group accounts for its equity investments over which it has significant influence but does not own a majority equity interest or otherwise control using the equity method. The Group adjusts the carrying amount of the investments and recognizes in earnings its share of the earnings or loss of the investee after the date of investment.

These investments are measured at fair value on a nonrecurring basis when there are events or changes in circumstances that may have a significant adverse effect. An impairment loss is recognized in the consolidated statements of comprehensive loss equal to the amount by which the carrying value exceeds the fair value of the investment.

(m) Revenue recognition

The Group follows five steps for its revenue recognition under Accounting Standard Codification ("ASC")606:

- Step 1: Identify the contract (s) with a customer
- Step 2: Identify the performance obligations in the contract
- Step 3: Determine the transaction price
- Step 4: Allocate the transaction price to the performance obligations in the contract
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation

The Group's revenue is reported net of discounts, value added tax and related surcharges. The primary sources of the Group's revenues are as follows:

Product revenues

The Group recognizes revenues from the sale of medicines, healthcare products and other wellness merchandise through its online platforms, including its internet website 1 Medicine Marketplace, cellular phone application, other online channels and its offline pharmacies mainly to individual consumers (the "B2C Business"). The Group also generates revenues from the sale of medicines to its pharmacy customers mainly through the online platform 1 Pharmacy (the "B2B Business").

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(m) Revenue recognition (Continued)

Under both B2C Business and B2B Business, revenues from product sales are recognized at the point in time when the delivery is made and when title and risk of loss transfers to the consumers and pharmacy customers. Revenues are measured at the amount of consideration the Group expects to receive in exchange for transferring products to consumers and pharmacy customers ("transaction price"). To the extent that the transaction price includes variable consideration, the Group estimates the amount of variable consideration that should be included in the transaction price utilizing the most likely amount method. Variable consideration is included in the transaction price if, in the Group's judgment, it is probable that a significant future reversal of cumulative revenue under the contract will not occur. The Group provides the right of return in circumstances when there is packing or delivery damage or other quality problems identified within 30 days which is considered to be a form of variable consideration. The Group estimates sales returns based on historical experience and based on such, the amount of sales returns accrual was insignificant as of December 31, 2020 and 2021.

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111, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2019, 2020 and 2021 (Amounts in thousands, except for share data and per share data, unless otherwise stated)

The Group voluntarily provides discount coupons through its websites during its marketing activities. These coupons are not related to prior purchases, and can only be utilized in conjunction with subsequent purchases on the Group's platforms. The coupons are recorded as a reduction of revenue at the time of use.

The Group enters into rebate programs where once certain conditions are met, and refunds the customer with cash in rare circumstances. Since 2021, the Group enters into another new program with certain B2B customers, to grant the controlling shareholder of the B2B customers (the "recipient") options, to obtain shares of a wholly owned subsidiary of the Group ("Yijianyikang"), which will be vested over a four-year period that 25% of the options vesting on the anniversary from the grant date each year, and subject to certain predetermined annual purchase targets. The recipient shall exercise all the vested options upon the completion of the Initial Public Offering ("IPO") of Yijianyikang or the recipient registered as a shareholder of Yijianyikang, otherwise, the recipient has the right to convert the vested options to ordinary shares of the Company at certain ratio, which may have a dilutive impact of EPS. The equity instruments granted in conjunction with selling goods are measured and classified under Topic 718 at grant-date fair value. In determining the fair value of the equity instruments granted, a market approach was applied. The Group estimates the variable consideration for these programs using the expected value method, which predicts the amount of the consideration based on the terms of the contract and available information and updates its estimates each reporting period. The impact on EPS and deferred revenue of the new program is not material for the year ended December 31, 2021.

Under both B2B and B2C Businesses the Group utilizes delivery service providers to deliver products to its consumers and pharmacy customers ("shipping activities") but the delivery service is not considered as a separate obligation as the shipping activities are performed before the consumers and pharmacy customers obtain control of the products. Therefore, shipping activities are not considered a separate promised service to the consumers and pharmacy customers, but rather are activities to fulfill the Group's promise to transfer the products and are recorded as fulfillment expenses.

Product revenues are recorded net of surcharges and value added tax ("VAT") ranging from 0% to 13% for different kinds of products based on the sales amount. Surcharges are sales related taxes representing the City Maintenance and Construction Tax and Education Surtax. The Group records revenues on a gross basis because the Group controls the products before they are transferred to the consumers and pharmacy customers determined on the basis that: (1) the Group is primarily responsible for fulfilling its promise to deliver the specified products to consumers and pharmacy customers; (2) the Group has inventory risk before the specified products are transferred to a consumers and pharmacy customers or after transfer of control to the consumers and pharmacy customers, and (3) the Group has discretion in establishing the price for the specified products.

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

Service revenues

Service revenues primarily consist of fees charged to third-party marketplace sellers for whom the Group acts as an agent to facilitate the marketplace sellers' online sales of their products through the online platforms 1 Medicine Marketplace and 1 Pharmacy, which is referred to as marketplace service ("MP") revenue. The Group has determined it is not the principal in the arrangement as it is not responsible to fulfill the order for the specified products, it does not bear the inventory risk for the products, nor does it have the ability to establish prices. The Group charges the marketplace sellers commission fees equal to an agreed percentage of the sales price of the product when a sale is completed and also charges market place sellers an annual non-refundable up-front fee for platform usage. The promise to the customer, which is the marketplace seller, is to arrange for the sale which is considered as one performance obligation. Therefore, the Group recognizes the up-front fee and commission at the point in time when the sale is completed. The Group also provided digital marketing service, supply chain management to customers and etc. (collectively referred to "other services"), and recognize over time when the customer simultaneously receives and consumes the benefits provided by the Group's performance, or recognize at a point in time when the customer obtains control of the goods and services.

Contract balances

Accounts receivable represents amounts invoiced and revenue recognized prior to invoicing when we have satisfied our performance obligation and have the unconditional right to payment.

The estimated inventories in-transit relating to estimated returns are contract assets included in inventories.

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Contract liabilities consist of advance payments, which were recorded in accrued expenses and other current liabilities.

(n) Cost of products sold

Cost of products sold consists of the purchase price of products and inbound shipping charges. The Group periodically receives rebates from certain vendors in the form of cash or credits that the Group can apply against trade amounts owed to vendors pursuant to a binding arrangement only if the Group completes a specified cumulative level of purchases or sales within a specified time period. The rebates do not represent a payment for assets or services delivered to the vendor or a reimbursement of costs incurred by the Group to sell vendors' products. The Group accounts for the rebates received from its vendors as a reduction to the price the Group pays for the products purchased and therefore records such amounts as a reduction of cost of products sold and inventory when recognized in the financial statements. Rebates are earned based on reaching minimum purchases or sales thresholds within a specified period, typically on a fiscal quarterly or annual basis. Cost of products does not include other direct costs related to cost of product sales such as shipping and handling expense, payroll and benefits of logistics staff, logistics centers rental expenses and depreciation expenses. Therefore, the Group's cost of products sold may not be comparable to other companies which include such expenses in their cost of products.

(o) Fulfillment expenses

Fulfillment expenses primarily consist of payroll, bonus and benefits of logistics staff, logistics centers rental expenses, depreciation expenses, shipping and handling expenses, and packaging expenses.

(p) Selling and marketing expenses

Selling and marketing expenses primarily consist of payroll, bonus and benefits of sales and marketing staff, advertising costs, agency fees and costs for promotional materials.

Advertising expenses are charged to the statements of comprehensive loss in the period incurred. The amounts of advertising expenses incurred were RMB30,447, RMB37,577 and RMB30,135 for the years ended December 31, 2019, 2020 and 2021, respectively.

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(q) Technology expenses

Technology expenses primarily consist of technology infrastructure expenses, payroll, bonus and benefits of the employees, and costs associated with the computer, storage and telecommunications infrastructure for use in technology department.

For internal and external use software, the Group expenses all costs incurred for the preliminary project stage and post implementation-operation stage of development, and costs associated with repair or maintenance of the existing platform. Costs incurred in the application development stage are capitalized and amortized over the estimated useful life. The amount of the Group's technology expenses qualifying for capitalization has been insignificant, and as a result, all development costs incurred for development of internal used software have been expensed as incurred.

(r) General and administrative expenses

General and administrative expenses primarily consist of payroll, bonus and benefit costs for corporate employees, legal, finance, rental expenses and other corporate overhead costs.

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(s) Government grants

Government grants represent rewards provided by the relevant PRC government authorities to the Group for tax refunds and support for investment in certain local districts, which are typically granted based on the amount of investments the Group made as well as income generated by the Group in such districts. Such subsidies allow the Group full discretion to utilize the funds and are used by the Group for general corporate purposes. Normally, the Group does not receive written confirmation from local governments indicating the approval of the cash subsidy before cash is received, and therefore cash subsidies are recognized when received and when all the conditions for their receipts have been satisfied. Government grants recognized were RMB358, RMB 5,036 and RMB 2,947 for the years ended December 31, 2019, 2020 and 2021, respectively, which were recorded in other operating income (expenses), net.

(t) Income taxes

Current income taxes are provided for in accordance with the laws of the relevant taxing authorities. As part of the process of preparing financial statements, the Group is required to estimate its income taxes in each of the jurisdictions in which it operates. The Group accounts for income taxes using the liability method. Under this method, deferred income taxes are recognized for tax consequences in future years of differences between the tax bases of assets and liabilities and their reported amounts in the financial statements at each year-end and tax loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates applicable for the differences that are expected to affect taxable income. Deferred tax assets are reduced by a valuation allowance when, based upon the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The Group applies the provisions of ASC Topic 740, Income Taxes (“ASC 740”), in accounting for uncertainty in income taxes. ASC 740 clarifies the accounting for uncertainty in income taxes by prescribing the recognition threshold a tax position is required to meet before being recognized in the financial statements. The Group has elected to classify interest and penalties related to an uncertain tax position (if and when required) as part of income tax expense in the consolidated statements of comprehensive loss. The Group does not have any unrecognized tax benefits for the years ended December 31, 2019, 2020 and 2021.

(u) Value added taxes

The Group’s PRC subsidiaries are subject to VAT at rates ranged from 0% to 13% on proceeds received from customers, and are entitled to a deduction for VAT already paid or borne on the products purchased by them. The VAT balance is recorded in other current assets or other current liabilities on the consolidated balance sheets.

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(v) Comprehensive income (loss)

Comprehensive income (loss) is defined to include all changes in equity except those resulting from investments by owners and distributions to owners. During the periods presented, comprehensive income (loss) is reported in the consolidated statements of comprehensive loss, and other comprehensive loss includes foreign currency translation adjustments and fair value change of available-for-sale debt securities.

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(w) Foreign currency translation

The reporting currency of the Group is the Renminbi (“RMB”). The functional currency of the Company and Yao Wang is the United States dollar (“US dollar”). The functional currency of all the other significant subsidiaries and the variable interest entities is RMB. The determination of the respective functional currency is based on the criteria of ASC 830, *Foreign Currency Matters*.

Monetary assets and liabilities denominated in currencies other than the applicable functional currencies are translated into the functional currencies at the prevailing rates of exchange at the balance sheet date. Nonmonetary assets and liabilities are re-measured into the applicable functional currencies at historical exchange rates. Transactions in currencies other than the applicable functional currencies during the year are converted into the functional currencies at the applicable rates of exchange prevailing at the transaction dates. Transaction gains and losses are recognized in the consolidated statements of comprehensive loss.

Assets and liabilities are translated from each entity’s functional currency to the reporting currency at the exchange rate on the balance sheet date. Equity amounts are translated at historical exchange rates, and revenues, expenses, gains and losses are translated using the average rate for the year. Translation adjustments are reported as cumulative translation adjustments and are shown as a separate component of accumulated other comprehensive loss in the consolidated statements of shareholders’ equity (deficit).

(x) Concentration of credit risk

Financial instruments that potentially expose the Group to concentration of credit risk consist primarily of cash and cash equivalents, restricted cash, short-term investments, accounts receivable and prepayments. The Group places its cash and cash equivalents, restricted cash and short-term investments with financial institutions with high-credit ratings and quality. Accounts receivable mainly consist of amounts receivable from B2B customers, product delivery service providers and payment processing service providers, which are all with good collection history. There are no significant concentrations of credit risk. With respect to prepayments, the Group performs on-going credit evaluations of the financial condition of these suppliers.

Concentration of customers

There were no customers individually representing 10% or more of revenues for the years ended December 31, 2019, 2020 and 2021.

There were no customers accounted for 10% or more of balances of accounts receivable as of December 31, 2020 and 2021.

Concentration of suppliers

There were no suppliers accounted for 10% or more of purchases for the years ended December 31, 2019, 2020 and 2021.

There were no suppliers accounted for 10% or more of balances of accounts payable as of December 31, 2020 and 2021.

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(y) Foreign currency risk

Renminbi (“RMB”) is not a freely convertible currency. The State Administration of Foreign Exchange, under the authority of the People’s Bank of China, controls the conversion of RMB into foreign currencies. The value of RMB is subject to changes in central government policies and to international economic and political developments affecting supply and demand in the China Foreign Exchange Trading System market. The cash and cash equivalents of the Group included aggregated amounts of RMB 1,071,366 and RMB 605,623, which were denominated in RMB, as of December 31, 2020 and 2021, respectively.

(z) Fair value

Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and

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liabilities required or permitted to be recorded at fair value, the Group considers the principal or most advantageous market in which it would transact and it considers assumptions that market participants would use when pricing the asset or liability.

The established fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The three levels of inputs may be used to measure fair value include:

Level 1 applies to assets or liabilities for which there are quoted prices in active markets for identical assets or liabilities.

Level 2 applies to assets or liabilities for which there are inputs other than quoted prices included within Level 1 that are observable for the asset or liability such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or liabilities in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which significant inputs are observable or can be derived principally from, or corroborated by, observable market data.

Level 3 applies to assets or liabilities for which there are unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the assets or liabilities.

When available, the Group uses quoted market prices to determine the fair value of an asset or liability. If quoted market prices are not available, the Group measures fair value using valuation techniques that use, when possible, current market-based or independently sourced market parameters, such as interest rates.

The estimated fair value of the Group's financial instruments of which the inputs used to value are classified as Level 2 and are not reported at fair value, including cash and cash equivalents, restricted cash, short-term investments, accounts receivable, other current assets, accounts payable, other current liabilities, approximates their carrying value due to their short-term nature.

As of December 31, 2021, information about inputs into the fair value measurement of the Group's assets and liabilities that are measured at fair value on a recurring basis in periods subsequent to their initial recognition is as follows:

	Fair Value as of December 31, 2021	Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Short-term investments	182,556	—	182,556	—

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(z) Fair value (Continued)

The fair values of wealth management products are the suggested redemption price provided by the investment bank or fund company that sells such financial products. There are observable and market-based inputs but not quoted prices in active markets for identical assets. If statements are not available, the Group will measure fair value using valuation techniques that use current market-based parameters, such as currency rates. The total gain recognized for change in fair values of short-term investments is RMB 9,635, RMB 970 and RMB 7,801 for the years ended December 31, 2019, 2020 and 2021.

The Group's equity investments in equity securities without readily determinable fair values, which do not qualify for net asset value ("NAV") practical expedient and over which the Group does not have the ability to exercise significant influence through the investments in common stock or in substance common stock, are accounted for under the measurement alternative in accordance with ASU 2016-01 "Recognition and Measurement of Financial Assets and Liabilities" (the "Measurement Alternative"). Under the Measurement Alternative, the carrying value is measured at cost, less any impairment, plus and minus changes resulting from observable price changes in orderly transactions for identical or similar investments. The Group recognized impairment losses of RMB 11,000, nil and nil related to equity investments without readily determinable fair values for the years ended December 31, 2019, 2020 and 2021, respectively.

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The Group measures equity method investments at fair value on a nonrecurring basis when they are deemed to be impaired. The fair values of these investments are determined based on valuation techniques using the best information available, and may include future performance projections, discount rate and other assumptions that are significant to the measurements of fair value. An impairment charge to these investments is recorded when the carrying amount of the investment exceeds its fair value and this condition is determined to be other-than-temporary. During the year ended December 2021, no impairment of equity method investments was recorded.

Certain non-financial assets are measured at fair value on a nonrecurring basis, including property, plant, and equipment, right-of-use assets, and intangible assets. They are recorded at fair value only when impairment is recognized by applying unobservable inputs such as forecasted financial performance, discount rate, and other significant assumptions to the discounted cash flow valuation methodology. For the years ended December 31, 2019, 2020 and 2021, there was no impairment recognized for non-financial assets.

(aa) Share-based compensation

Awards Granted to Employees

The Group grants share options and restricted share units of the Company and its subsidiary to eligible employees and accounts for these share based awards in accordance with ASC 718 Compensation-Stock Compensation.

Employees' share-based awards are measured at the grant date fair value of the awards and recognized as expenses a) immediately at grant date if no vesting conditions are required; or b) using straight-line vesting method over the requisite service period, which is the vesting period. To the extent the required vesting conditions are not met resulting in the forfeiture of the share-based awards, previously recognized compensation expense relating to those awards are reversed.

Prior to the IPO of the Company on September 12, 2018, the fair value of the stock options granted to employees is determined with the assistance of an independent third party valuation firm. After the IPO of the Company, in determining the fair value of the share options and Ordinary Share Units of the Group, the closing market price of the underlying shares on the grant date is applied. The Black Scholes option pricing model was applied in determining the estimated fair value of the options granted to employees. In determining the fair value of the restricted shares of limited liability partnerships ("LLPs"), market approach and income approach were applied for the years ended December 31, 2020 and 2021, respectively.

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(aa) Share-based compensation (Continued)

The Group estimates the Company's subsidiary's enterprise value for purposes of recording share-based compensation, and the information considered by the Company mainly include but are not limited to the pricing of recent rounds of financing, future cash flow forecasts, discount rates, and liquidity factors.

The compensation expense for the awards with performance conditions is based upon the Group's judgement of likely future performance and may be adjusted in future periods depending on actual performance.

Awards Granted to Non-Employees

The Group adopted ASU 2018-07 on January 1, 2019 using the modified retrospective method and recognized the cost of services received from a nonemployee in exchange for an equity instrument based on the award's grant-date fair value. Unvested equity-based payments to nonemployees have been re-measured at fair value as of the adoption date. The adoption did not have material effect on the financial statements.

(ab) Treasury shares

Treasury shares represent shares repurchased by the Company that are no longer outstanding and are held by the Company. Treasury shares are accounted for under the cost method. Under the repurchase plan, the Company had repurchased an aggregate of

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1,485,862, 511,758 and 333,000 ordinary shares on the open market for total cash consideration of RMB 22,991, 11,981 and 5,887 for the year ended December 31, 2019, 2020 and 2021. The repurchased shares are presented as “treasury shares” in shareholders’ equity on the Group’s consolidated balance sheets.

(ac) Earnings (loss) per share

Basic earnings (loss) per ordinary share is computed by dividing net income (loss) attributable to ordinary shareholders by weighted average number of ordinary shares outstanding during the period.

Diluted earnings (loss) per ordinary share reflects the potential dilution that could occur if securities were exercised or converted into ordinary shares. The Group has stock options and restricted share units, which could potentially dilute basic earnings per share in the future. To calculate the number of shares for diluted income per share, the effect of the stock options and restricted share units is computed using the treasury stock method. Ordinary share equivalents are excluded from the computation of the diluted earnings (loss) per share in years when their effect would be anti-dilutive.

In September 2018, the Company’s shareholders voted in favor of a proposal to adopt a dual-class share structure, pursuant to which the Company’s authorized share capital were reclassified and redesigned into Class A ordinary shares and Class B ordinary shares (Note 13). Both Class A ordinary shares and Class B ordinary shares are entitled to the same dividend right, as such, this dual class share structure has no impacts to the earnings per share calculation. Basic earnings per share and diluted earnings per share are the same for each Class A ordinary shares and Class B ordinary shares.

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)***(ad) Segment reporting***

In accordance with ASC 280, Segment Reporting, the Group’s chief operating decision maker (the “CODM”) has been identified as the Co-Chairmen and Chief Executive Officer, who review the segment information when making decisions about allocating resources and assessing performance of the Group. The Group classifies its operations into two segments: B2C segment and B2B segment whereby the B2C business represents revenue generated from individual consumers while B2B business represents revenue generated from corporate customers. There are no internal revenue transactions between the reportable segments. The Group does not distinguish expenses between segments in its internal reporting, and reports expenses by nature as a whole. Furthermore, the Group’s CODM is not provided with asset information by segment. As such, no asset information by segment is presented. The information of segment reporting is presented consistently for the years ended December 31, 2019, 2020 and 2021. The following tables summarize the Group’s product revenues and segment profit (loss) generated by its segments.

	Year Ended December 31,		
	2019	2020	2021
B2C segment			
Product revenues	636,430	666,223	491,855
Service revenues	17,818	25,043	30,896
Cost of products sold*	(535,577)	(551,998)	(413,333)
Segment profit for B2C Business	118,671	139,268	109,418
B2B segment			
Product revenues	3,293,268	7,490,449	11,839,850
Service revenues	4,537	21,442	63,301
Cost of products sold*	(3,251,293)	(7,285,327)	(11,391,474)
Segment profit for B2B Business	46,512	226,564	511,677
Total segment profit	165,183	365,832	621,095

* For segment reporting purpose, purchase rebate is allocated to B2C segment and B2B segment primarily based on the amount of cost of products sold for each segment. Cost of products sold does not include other direct costs related to cost of product sales such as

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shipping and handling expense, payroll and benefits of logistic staff, logistic centers rental expenses and depreciation expenses, which are recorded in the fulfillment expenses.

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(ad) Segment reporting (Continued)

The following is a reconciliation of the reportable segments' measures of profit or loss to the Group's consolidated loss before income taxes:

	Year Ended December 31,		
	2019	2020	2021
Total profit for reportable segments	165,183	365,832	621,095
Unallocated amounts:			
Fulfillment expenses	(128,996)	(226,930)	(355,836)
Selling and marketing expenses	(340,562)	(399,610)	(513,146)
General and administrative expenses	(123,501)	(128,226)	(206,981)
Technology expenses	(61,902)	(92,080)	(189,284)
Other operating (expenses) income, net	(3,735)	7,703	2,012
Interest income	4,802	6,312	9,776
Interest expense	(3,622)	(8,817)	(5,488)
Foreign exchange (loss) gain	(10,328)	5,547	1,937
Other income, net	834	3,161	14,890
Loss before income tax	<u>(501,827)</u>	<u>(467,108)</u>	<u>(621,025)</u>

Revenues from different product groups and services are as follows:

	Year Ended December 31,		
	2019	2020	2021
Product Revenues			
Drugs	3,929,698	8,156,672	12,331,705
Nutritional supplements	3,595,419	7,398,433	11,681,106
Contact lenses.	245,644	559,239	442,497
Medical supplies and devices	18,110	3,420	38
Other products.	50,178	149,051	124,919
Service Revenues	22,355	46,485	94,197
MP Service	20,347	46,529	83,145
Other Services	5,116	15,952	41,888
Total	<u>3,952,053</u>	<u>8,203,157</u>	<u>12,425,902</u>

(ae) Leases

From January 1, 2019, the Group adopted the ASC Topic 842, Leases ("ASC 842"). The Group determines if a contract is or contains a lease at the inception of the contract, and the Group classifies that lease as a finance lease if it meets certain criteria or as an operating lease when it does not. For a contract, in which the Group is a lessee, that contains fixed payments for both lease and non-lease components, the Group has elected to account for lease and non-lease components separately.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(ae) Leases (Continued)

At the commencement date of a lease, the Group recognizes a lease liability for future fixed lease payments and a right-of-use (“ROU”) asset representing the right to use the underlying asset during the lease term. The lease liability is initially measured as the present value of the future fixed lease payments that will be made over the lease term. The lease term includes lessee options to extend the lease and periods occurring after a lessee early termination option, only to the extent it is reasonably certain that the Group will exercise such extension options and not exercise such early termination options, respectively. The future fixed lease payments are discounted using the rate implicit in the lease, if available, or the incremental borrowing rate (“IBR”). The Group’s IBR is estimated to approximate the interest rate on similar terms and payments and in economic environments where the leased asset is located. Upon adoption of ASU 2016-02, the Group elected to use the remaining lease term as of January 1, 2019 in the Group’s estimation of the applicable discount rate for leases that were in place at adoption. For the initial measurement of the lease liability for leases commencing after January 1, 2019, the Group used the discount rate as of the commencement date of the lease, incorporating the entire lease term. Additionally, the Group elected not to recognize leases with lease terms of 12 months or less at the commencement date in the consolidated balance sheets. Current maturities and long-term portions of operating lease liabilities are classified as accrued expenses and other current liabilities and long-term operating lease liabilities, respectively, in the consolidated balance sheets.

The ROU asset is measured at the amount of the lease liability with adjustments, if applicable, for lease prepayments made prior to or at lease commencement, initial direct costs incurred by the Group and lease incentives. The Group will evaluate the carrying value of ROU assets if there are indicators of impairment and review the recoverability of the related asset group. If the carrying value of the asset group is determined to not be recoverable and is in excess of the estimated fair value, the Group will record an impairment loss in other expenses in the consolidated statements of operations. ROU assets for operating leases are included in operating lease right-of-use assets in the consolidated balance sheets. For the years ended December 31, 2019, 2020 and 2021, there were no impairment recognized for the Group’s ROU assets.

The Group’s leases include offices and warehouses, which are all classified as operating leases with fixed lease payments, or minimum payments, as contractually stated in the lease agreement. For operating leases, lease expense relating to fixed payments is recognized on a straight-line basis over the lease term.

(af) Non-controlling interests

For the Company’s consolidated subsidiaries and VIEs, non-controlling interests are recognized to reflect the portion of their equity that is not attributable, directly or indirectly, to the Company as the controlling shareholder. Non-controlling interests are classified as a separate line item in the equity section of the Group’s consolidated balance sheets and have been separately disclosed in the Group’s consolidated statements of operations and comprehensive income/(loss) to distinguish the interests from that of the Company.

(ag) Redeemable non-controlling interest

The Group classifies the redeemable non-controlling interest as mezzanine equity as the non-controlling interest is redeemable upon the occurrence of an event not solely within the control of the Group.

Due to the probability of being redeemed, the Group adjusts the carrying amount of the mezzanine equity to equal the redemption value at the end of each reporting period as if it was the redemption date for the redeemable non-controlling interest. The balance of the redeemable non-controlling interest is reported at the greater of the initial carrying amount adjusted for the redeemable non-controlling interest’s share of earnings or losses and other comprehensive income or loss, or its estimated redemption value. The resulting changes in the estimated redemption amount (increases or decreases) are recorded in net loss or profit attributable to non-controlling interests. These interests are presented on the consolidated balance sheets outside of equity under the caption “Redeemable non-controlling interest”.

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2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

(ah) Recently issued accounting pronouncements

New Accounting Pronouncements Not Yet Adopted

In November 2021, the FASB issued ASU 2021-10, Government Assistance (Topic 832) — Disclosures by Business Entities about Government Assistance. The amendments in this ASU require disclosures about transactions with a government that have been accounted for by analogizing to a grant or contribution accounting model to increase transparency about (1) the types of transactions, (2) the accounting for the transactions, and (3) the effect of the transactions on an entity's financial statements. The amendments in this ASU are effective for all entities within their scope for financial statements issued for annual periods beginning after December 15, 2021. Early application of the amendments is permitted. The Group does not expect the adoption of this new standard to have any material impact on its financial statements.

(ai) Convenience translation

Translations of balances in the consolidated balance sheets, consolidated statements of comprehensive loss, and consolidated statements of cash flows from RMB into US dollar as of and for the year ended December 31, 2021 are solely for the convenience of the readers and were calculated at the rate of 6.3726, representing the noon buying rate set forth in the H.10 statistical release of the U.S. Federal Reserve Board on December 30, 2021. No representation is made that the RMB amounts could have been, or could be, converted, realized or settled into US dollar at that rate on December 30, 2021, or at any other rate.

(aj) Structured payment arrangement

In 2021, the Group entered into a structured payment arrangement with a bank ("reverse factoring arrangement"). Under the reverse factoring arrangement, certain suppliers were able to put their receivables from the Group to the bank for early payment.

As a result of the reverse factoring arrangements, the payment terms of the Group's original accounts payables were substantially modified and considered extinguished as the nature of the original liability has changed from accounts payables to loan borrowings from the bank. The proceeds from the bank used to settle the payables and subsequent repayments to the bank are considered financing activities and reported as "Proceeds from other financing activities" and "Repayment for other financing activities" on the consolidated statements of cash flows, respectively. The interest expense charged from the bank at annual rate of 4.35%, is recorded in interest expense in the consolidated statements of comprehensive loss. As of December 31, 2021, the outstanding borrowings from the reverse factoring arrangements were RMB 46,900, which is repayable within one year and are included in "Accrued expenses and other current liabilities" on the consolidated balance sheets. Total proceeds obtained for settlement for the year ended December 31, 2021, was RMB61,900, and were typically repayable within 90 days of issuance.

3. SHORT-TERM INVESTMENTS

Short-term investments as of December 31, 2020 and 2021 were as follows:

	As of December 31,	
	2020	2021
Wealth Management Products	300,167	182,556

The Group classifies the wealth management products as "available-for-sale" debt securities which are recorded at fair value. For the years ended December 31, 2019, 2020 and 2021, the Group recorded RMB 7,335, RMB 1,137 and RMB 8,312 of changes in fair value of these available-for-sale debt securities, net of tax, in other comprehensive income (loss), respectively, and RMB 9,635, RMB 970 and RMB 7,801 of realized gains transferred from other comprehensive income to other income when the security was sold. The amortized cost of the available-for-sale debt securities approximate their fair value. No impairment charges were recorded for the year ended December 31, 2019, and no credit loss was recognized for the years ended December 31, 2020 and 2021.

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4. NOTES RECEIVABLE

As of December 31, 2020 and 2021, the total note receivable balance was RMB12,583 and RMB90,734 and among which RMB5,969 and RMB7,181 were pledged as collateral for notes payable which is recorded in accounts payables. No impairment charges were recorded for the year ended December 31, 2019, and no credit loss was recognized for the years ended December 31, 2020 and 2021.

5. INVENTORIES

Inventories as of December 31, 2020 and 2021 were as follows:

	As of December 31,	
	2020	2021
Products	766,529	1,121,107

In 2020 and 2021, inventories were written down by RMB24,216 and RMB45,976, respectively, to reflect the lower of cost and net realizable value.

6. PREPAYMENTS AND OTHER CURRENT ASSETS

Prepayment and other current assets, as of December 31, 2020 and 2021 were as follows:

	As of December 31,	
	2020	2021
Value added tax recoverable	149,343	92,107
Rebate receivable from suppliers	114,723	77,687
Deposits (Note)	25,600	35,905
Advance to suppliers	9,891	21,064
Prepaid expense	8,117	9,476
Others	4,123	5,960
Total	311,797	242,199

Note: Deposits consist of amounts paid to certain vendors for purchasing, advertising and rentals.

7. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	As of December 31,	
	2020	2021
Cost:		
Leasehold improvements	55,941	91,908
Electronic equipment	25,857	36,008
Furniture, fixtures and equipment	21,334	35,546
Vehicles	943	1,026
	104,075	164,488
Less: Accumulated depreciation	(60,636)	(84,234)
	43,439	80,254
Construction in progress	—	—
Property and equipment, net	43,439	80,254

Depreciation expense was RMB10,607, RMB12,223 and RMB25,513 for the years ended December 31, 2019, 2020 and 2021, respectively.

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8. LEASES

The Group has operating leases for offices and warehouses. The Group recognized ROU assets of RMB 98,628 and RMB 233,847, and corresponding current liabilities of RMB 37,713 and RMB 65,740 in accrued expenses and other current liabilities, and long-term operating lease liabilities of RMB 62,388 and RMB 165,614, as of December 31, 2020 and 2021. The amount of short-term is not material and no variable lease cost existed for the years ended December 31, 2019, 2020 and 2021, respectively.

Lease expenses were RMB 29,715, RMB 41,936 and RMB 73,756 for the year ended December 31, 2019, 2020 and 2021. The maturities of lease liabilities in accordance with *Leases (Topic 842)* in each of the next five years and thereafter as of December 31, 2020 and 2021 were as follows:

Year Ending December 31,	As of December 31,	
	2020	2021
2021	41,893	—
2022	32,006	73,723
2023	15,602	66,932
2024	11,507	59,633
2025	7,857	42,059
2026	616	6,914
Thereafter	—	205
Total lease payment	109,481	249,466
Less: imputed interest	(9,380)	(18,112)
Present value of minimum operating lease payments	<u>100,101</u>	<u>231,354</u>

Cash paid for amounts included in the measurement of operating lease liabilities for the years ended 31 December, 2019, 2020 and 2021 were RMB 29,042, RMB 40,792 and RMB 77,722. Right-of-use assets obtained in exchange for the operating lease liabilities in non-cash transactions for the years ended 31 December, 2020 and 2021 were RMB 50,841, RMB 50,076 and RMB 225,003. Right-of-use assets decreased due to lease early termination for the years ended 31 December, 2019, 2020 and 2021 were nil, RMB 1,685 and RMB 23,624.

Weighted-average remaining lease terms and discount rates are as follows:

	As of December 31,	
	2020	2021
Weighted-average remaining lease term	3.2 years	3.6 years
Weighted-average discount rate	5.0 %	4.3 %

9. SHORT-TERM BORROWINGS

Short-term borrowings were RMB 229,250 and RMB 259,658 as of December 31, 2020 and 2021, respectively, all of which consisted of borrowings from financial institutions and are repayable within one year. As of December 31, 2021, the Group had an undrawn balance of RMB 270,342 under the credit facilities agreement. All of these borrowings were unsecured and accrue interest at an average annual interest rate of 5.32% and 4.35% for the years ended December 31, 2020 and 2021, respectively.

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9. SHORT-TERM BORROWINGS (Continued)

In September 2019, 1 Pharmacy Technology entered into a credit agreement with China Merchant Bank (CMB) which provides a revolving credit facility that allows 1 Pharmacy Technology to borrow up to RMB 100,000 for working capital purpose in one year. In October 2020, 1 Pharmacy Technology renewed the credit agreement that allowed 1 Pharmacy Technology to borrow up to RMB 300,000 for working capital purposes in one year, and in November 2021, 1 Pharmacy Technology renewed the credit agreement for another one year. Any draw down on the credit facility will be charged with interest at one-year loan prime rate published by People's Bank of China plus 0.30%. The borrowings were guaranteed by Yihao Pharmacy. During the year ended December 31, 2020 and 2021, RMB229,666 and RMB331,837 were drawn on above credit facility and RMB159,666 and RMB232,179 were repaid, with the balance of RMB100,000 and RMB199,658 outstanding as of December 31, 2020 and 2021, respectively. The interest rate range for the borrowings in 2020 and 2021 were from 4.10% to 4.35 % per annum.

In June 2020, 1 Pharmacy Technology entered into a credit agreement with Industrial Bank (IB) which provides a revolving credit facility that allows 1 Pharmacy Technology to borrow up to RMB 100,000 for working capital purpose in one year. Any draw down on the credit facility will be charged with interest at one-year loan prime rate published by People's Bank of China minus 0.35%. In June 2021, the credit agreement was renewed and allows 1 Pharmacy Technology to borrow up to RMB 200,000 for working capital purpose in seven months. Any draw down on the credit facility will be charged with interest at one-year loan prime rate published by People's Bank of China plus 0.78%. The borrowings in the years ended December 31, 2020 and 2021 were guaranteed by Yihao Pharmacy. During the years ended December 31, 2020 and 2021, RMB 9,850 and RMB 30,000 were drawn on this credit facility , RMB 9,850 were repaid in 2021, with the balance of RMB 9,850 and RMB 30,000 outstanding as of December 31, 2020 and 2021, respectively.

The Group entered into a revolving credit facility with China Zheshang Bank (CZB) that allows the Group to borrow up to RMB 500,000 for working capital purpose since December 2018 and renewed in December 2020 which will expire in two years. Cash deposits or notes receivable are required to be pledged for any draw down of borrowings and notes payables from CZB. During 2020, Yihao Pharmacy repaid RMB 65,081 borrowed from China Zheshang Bank (CZB) with no balance outstanding as of December 31, 2020. The interest rate for the borrowings in 2020 was 4.35% per annum. No loan with China Zheshang Bank (CZB) was entered in 2021. 1 Pharmacy Technology obtained loan of RMB 40,000 from Shanghai Pudong Technology Financial Service Co., Ltd. with annual interest rate of 8.5% in May 2020. The borrowing was guaranteed by Yihao Pharmacy. 1 Pharmacy Technology repaid RMB 40,000 in 2021 with no balance outstanding as of December 31, 2021. 1 Pharmacy Technology also borrowed RMB 10,000 from China Construction Bank (CCB) in 2020 and paid back in 2021. The loan agreement with CCB includes covenants that Debt to Asset Ratio of 1 Pharmacy Technology should be no more than 70%, and the Liquidity Ratio should be no less than 1.0. 1 Pharmacy Technology was in compliance with the covenants as of payment due date in 2021.

The Group also obtained loans from several other financial institutions. During the years ended December 31, 2020 and 2021, RMB109,250 and RMB45,000 were borrowed, RMB39,850 and RMB84,400 were repaid, with the balance of RMB69,400 and RMB30,000 outstanding as of December 31, 2020 and 2021, respectively. The interest rate range for the borrowings was from 3.50% to 4.60% per annum in 2020 and 4.15 % to 4.60% per annum in 2021.

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10. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities as of December 31, 2020 and 2021 were as follows:

	As of December 31,	
	2020	2021
Advance from customers	117,451	176,256
Salary and welfare payables	53,731	74,886
Current portion of operating lease liabilities	37,713	65,740
Payable to marketplace sellers (Note)	29,867	48,362
Liability under reverse factoring program	—	46,900
Deposits from marketplace sellers	13,564	26,307
Accrued delivery service fees	21,108	27,198
Accrued fulfillment expenses	13,274	12,545
Tax payables	9,576	10,935
Accrued advertising expense	3,244	3,794
Others	27,590	30,045
Total	<u>327,118</u>	<u>522,968</u>

Note: Amounts relate to cash collected on behalf of marketplace sellers for products sold through the Group's online platform.

11. REDEEMABLE NON-CONTROLLING INTERESTS

In August and December, 2020, 1 Pharmacy Technology issued its ordinary shares to certain private placement investors at fair value evaluated by the third party valuer, representing 9.2% of the outstanding shares of 1 Pharmacy Technology for total consideration of RMB 934,820. Under the agreements, 1 Pharmacy Technology and the new investors agreed to facilitate 1 Pharmacy Technology's IPO in the Shanghai Sci-Tech Innovation Board ("STAR") prior to June 30, 2023. If the IPO has not been completed and the China Securities Regulatory Commission has not otherwise approved the registration of the STAR Listing registration application prior to June 30, 2023, the new investors have the right to require Yao Wang to repurchase all or any portion of their ownership interests in 1 Pharmacy Technology at the cost plus annual interest rate of 6%. The ownership interests held by the new investors were classified as redeemable non-controlling interests under ASC 480 Distinguishing Liabilities from Equity as the redemption feature embedded in the non-controlling interests and not solely within the Group's control. Total number of 66,318,885 shares was increased in Yao Wang's redeemable non-controlling interests due to issuance of common stock of 1 Pharmacy Technology.

Based on the IPO process of 1 Pharmacy Technology, in 2021, the Group assessed the exercisability of the redemption right to be probable from June 30, 2023. For the year ended December 31, 2021, RMB56,766 attribution was recorded under ASC 810 as net loss attributable to redeemable non-controlling interest, and RMB133,370 of difference between carrying amount and redemption value was recorded under ASC 480 as adjustment attributable to redeemable non-controlling interest.

The redeemable non-controlling interests for the year ended December 31, 2021 was summarized as follows:

	Amount
Opening balance as of January 1, 2021	924,245
Net loss attributable to the redeemable non-controlling interests shareholders	(56,766)
Accretion of redeemable non-controlling interest	133,370
Ending balance as of December 31, 2021	<u>1,000,849</u>

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12. NON-CONTROLLING INTERESTS

In November 2020, the Company's subsidiary, 1 Pharmacy Technology issued 32,500,000 ordinary shares to 13 LLPs founded by the employees of 1 Pharmacy Technology with the total consideration of RMB 32,500. With full shareholders' rights of these ordinary shares issued to the LLPs, these shares are accounted as non-controlling interest of 1 Pharmacy Technology. The shares issued to the employees in each LLP are not outstanding shares but are restricted with 50% of the shares vesting within two years from the issuance date and the remaining 50% vesting evenly on an annual basis over the 2 years thereafter, which are also subject to adjustment based on performance condition. Such arrangement was entered into to provide a share incentive plan to the employees of 1 Pharmacy Technology. Share-based compensation was recognized over the vesting period based on the excess of the fair value of these shares over the issuance price (see Note 15).

Non-controlling interest ("NCI") was recognized at RMB 51,728 based on the proportional net assets of 1 Pharmacy Technology, with the difference of RMB19,228 recognized as a deduction to additional paid in capital as of December 31, 2020. For the year ended December 31, 2021, RMB27,819 was recorded as net loss attributable to the non-controlling interests shareholders.

13. ORDINARY SHARES

As of January 1, 2018, the authorized shares consist of 72,000,000 Class A ordinary shares, 839,209,895 Class B ordinary shares, and 13,671,109 Class C ordinary shares. In 2015 and 2016, the Group issued total of 1,607,901 Class C Ordinary Shares to Gold Prized Investment Limited ("Gold Prized") to establish a reserve pool for future issuance of equity share incentive to the Group's employees. While these ordinary shares were legally issued to Gold Prized, the voting rights and associated economic rights remained with the Group. As such, none of these ordinary shares were considered to be granted under the incentive plan, and the Company accounted for these shares as issued but not outstanding. In June 2018, Gold Prized irrevocably surrendered these 1,607,901 Class C ordinary shares ("Surrendered Shares") registered under its name to the Group resulting in the cancellation of the related subscription receivable of RMB2,200, which has no effect on the Group's total equity (deficit) amount. The Surrendered Shares were cancelled with effect from June 2018 and the Company reserved those shares in the authorized share capital to be issued pursuant to the Plan.

In September 2018, with the effectiveness of the revised Articles of Association, the Company's authorized share capital was changed to US\$50 divided into 1,000,000,000 shares comprising (i) 800,000,000 Class A ordinary shares of a par value of US\$0.00005 each, (ii) 72,000,000 Class B ordinary shares of a par value of US\$0.00005 each and (iii) 128,000,000 shares of a par value of US\$0.00005 each of such class or classes as Company's board of directors may determine. All 72,000,000 issued and outstanding Class A ordinary shares beneficially owned by Dr. Gang Yu and Mr. Junling Liu were re-designated as Class B ordinary shares, and all other issued and outstanding shares were re-designated as Class A ordinary shares. Each Class A ordinary share entitles the holder to one vote, and each Class B ordinary share entitles the holder to fifteen votes on all matters subject to the vote at general meetings of the Company. Both Class A ordinary shares and Class B ordinary shares are entitled to the same dividend right, as such, this dual class share structure has no impacts to the earnings per share calculation. Basic earnings per share and diluted earnings per share are the same for each Class A ordinary share and Class B ordinary share. In September 2018, 75,118,996 preferred shares were converted into Class A ordinary shares and the Company issued 15,969,110 Class A ordinary shares with the completion of the IPO.

On January 25, 2019, 5,500,000 Class A ordinary shares were issued to the Company's depositary bank, Bank of New York Mellon ("BNYM"), for bulk issuance of ADSs reserved for future issuances restricted stocks upon the exercise of stock options or vesting of restricted stocks under the 2013 Share Incentive Policy, 2014 Share Incentive Policy, 2016 Share Incentive Plan and 2018 Share Incentive Plan (together, the "Plans"). From August 15, 2019 to August 14, 2020, the Company repurchased a total of 1,997,620 Class A ordinary shares of the Company and the repurchased shares were transferred to Computershare Hong Kong Investor Services Ltd. ("Computershare"), also for future issuances upon the exercise of stock options or vesting of restricted stocks under the Plans.

For the years ended December 31, 2019, 2020 and 2021, 2,517,780, 1,745,136 and 1,128,084 Class A ordinary shares were issued and outstanding upon the exercise of stock options and vesting of restricted stocks, and an aggregated of 1,485,862, 511,758 and 333,000 shares were repurchased under the repurchase plan respectively.

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14. NET REVENUES

Disaggregation of revenues

All of the Group's revenues for the years ended December 31, 2019, 2020 and 2021 were generated within the PRC. The following table illustrates the disaggregation of the Group's revenue streams by type of customers and nature of services the Group offered:

	Year Ended December 31,		
	2019	2020	2021
Product Revenues	3,929,698	8,156,672	12,331,705
B2C Business	636,430	666,223	491,855
B2B Business	3,293,268	7,490,449	11,839,850
Service Revenues	22,355	46,485	94,197
MP Service	17,239	30,533	52,309
Other Services	5,116	15,952	41,888
Total	3,952,053	8,203,157	12,425,902

The revenues by different product groups and services has been disclosed in Note 2(ad).

Contract balance

The typical contract term of MP service is no more than one year and the remaining unsatisfied performance obligation as of December 31, 2020 and 2021 was insignificant.

In some arrangements from which product revenue is generated, the Group receives advance payments from consumers and pharmacy customers before the product is delivered, which is recorded as advance from customers included in the accrued expenses and other current liabilities on the consolidated balance sheets. The movements of the Group's accounts receivable and advances from customers are as follows:

	Accounts Receivable	Advances from Customers
Ending Balance as of December 31, 2019	65,247	63,456
Increase/(decrease), net	97,847	53,995
Ending Balance as of December 31, 2020	163,094	117,451
Increase/(decrease), net	241,375	58,805
Ending Balance as of December 31, 2021	<u>404,469</u>	<u>176,256</u>

Revenues with amount of RMB 63,456 and RMB 117,451 were recognized in the years ended December 31, 2020 and 2021, respectively that were included in the balance of advance from customers at the beginning of the each year.

15. SHARE-BASED COMPENSATION

Employee Share options

In September 2013, the Board of Directors of the Company approved an Equity Incentive Plan (the "Plan"), under which, the Board of Directors may grant options to purchase ordinary shares to officers and directors, employees and individual advisors who render services to the Group to purchase an aggregate of no more than 1,287,500 ordinary shares of the Group ("Option Pool"). From 2014 to 2021, the Board of Directors approved to increase the Option Pool to 16,943,190 ordinary shares.

The options granted have a contractual term of 10 years and generally vest over a four-year period, with vesting schedules: 25% of the awards vesting on the anniversary of the grant date each year.

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15. SHARE-BASED COMPENSATION (Continued)*Employee Share options (Continued)*

The Black Scholes model was applied in determining the estimated fair value of the options granted. The model requires the input of subjective assumptions. The following table presents the assumptions used to estimate the fair values of the share options granted for the years ended December 31, 2019, 2020 and 2021:

	2019	2020	2021
Risk-free rate of return	1.68%~2.63%	0.10%-1.67%	0.84%
Contractual life of option	10 years	10 years	10 years
Expected term	6.25 years	6.25 years	6.25 years
Estimated volatility rate	30%~41%	34%-59%	39%
Dividend yield	Nil	Nil	Nil
Fair value per ordinary share	US\$2.37~\$3.40	US\$2.95~\$3.74	US\$3.08

A summary of employee option activity under the Plan during the years ended December 31, 2019, 2020 and 2021 is presented below:

	Number of Options	Weighted average exercise price	Weighted average remaining contractual term	Aggregate intrinsic value	The weighted-average grant-date fair value of the options
	US\$	Years	US\$	US\$	
Outstanding at January 1, 2019	8,890,629	1.76	8.28	36,888	
Granted	1,063,293	4.12			0.49
Forfeited	(2,086,050)	1.99			
Expired	—	—			
Exercised	(1,962,484)	0.76		3,220	
Outstanding at December 31, 2019	5,905,388	2.44	7.96	22,807	
Granted	965,000	2.58			1.06
Forfeited	(247,232)	2.10			
Expired	—	—			
Exercised	(325,190)	1.62		1,260	
Outstanding at December 31, 2020	6,297,966	2.52	7.32	21,389	
Granted	146,426	5.25			0.70
Forfeited	(355,175)	0.34			
Expired	—	—			
Exercised	(233,096)	1.94		588	
Outstanding at December 31, 2021	5,856,121	2.55	6.32	349	
Vested and exercisable as of December 31, 2021	4,136,123	2.36	5.94	335	
Vested or expected to vest as of December 31, 2021	5,856,121	2.55	6.32	349	

Total compensation cost recognized for the years ended December 31, 2019, 2020 and 2021 was RMB 36,633 , RMB 37,662 and RMB 25,565.

As of December 31, 2021, there was RMB6,893 of unrecognized compensation expense related to unvested share options, which is expected to be recognized over a weighted average period of 1.3 years.

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15. SHARE-BASED COMPENSATION (Continued)

Non-Employee Share options

The options granted have a contractual term of 10 years and were issued in payment for their consultation services which was expected to be performed over 4 years from the date of issuance. As services are performed, 25% of the awards vest on the anniversary of the grant date each year. The estimated fair value of the awards were determined using the Black Scholes model with the same assumptions used in employee share options.

The following table presents the assumptions used to estimate the fair values of the share options granted for the years ended December 31, 2019, 2020 and 2021:

	Number of Options	Weighted average exercise price US\$	Weighted average remaining contractual term Years	Aggregate intrinsic value US\$	The weighted-average grant-date fair value of the options US\$
Outstanding at January 1, 2019	1,106,587	0.62	6.18	664	—
Granted	—	—			
Forfeited	—	—			
Expired	—	—			
Exercised	<u>(254,068)</u>	0.60		115	
Outstanding at December 31, 2019	852,519	0.62	5.23	549	—
Granted	—	—			
Forfeited	—	—			
Expired	—	—			
Exercised	<u>(781,894)</u>	0.50		211	
Outstanding at December 31, 2020	70,625	1.99	6.83	338	—
Granted	—	—			
Forfeited	—	—			
Expired	—	—			
Exercised	—	—			
Outstanding at December 31, 2021	<u>70,625</u>	<u>1.99</u>	<u>5.83</u>	<u>—</u>	<u>—</u>
Vested and exercisable as of December 31, 2021	61,875	1.99	5.76	—	—
Vested or expected to vest as of December 31, 2021	<u>70,625</u>	<u>1.99</u>	<u>5.83</u>	<u>—</u>	<u>—</u>

Total compensation cost recognized for the years ended December 31, 2019, 2020 and 2021 was a reduction of RMB 511 due to adoption of ASU 2018-07, RMB 111 and RMB 87, respectively.

As of December 31, 2021, there was RMB20 of unrecognized compensation expense related to unvested share options, which is expected to be recognized over a weighted average period of 0.1 year.

Restricted share units

The restricted share units granted have a contractual term of 10 years and vest over a four-year period that 25% of the awards vesting on the anniversary of the grant date each year. The fair value of restricted share units with service conditions or performance conditions is based on the fair market value of the underlying ordinary shares on the date of grant.

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15. SHARE-BASED COMPENSATION (Continued)

Restricted share units (Continued)

The following table summarized the Group's restricted share unit activities in 2019, 2020 and 2021.

	Number of Restricted Share Units	Weighted Average Grant Date Fair Value	
		US\$	US\$
Restricted share units outstanding at January 1, 2019	—	—	—
Granted	3,050,427	3.90	
Forfeited	(195,200)	3.10	
Vested	(301,228)	4.60	
Restricted share units outstanding at January 1, 2020	2,553,999	3.88	
Granted	1,716,950	3.28	
Forfeited	(565,116)	2.83	
Vested	(638,052)	4.12	
Restricted share units outstanding at December 31, 2020	3,067,781	3.69	
Granted	1,552,040	5.27	
Forfeited	(1,339,044)	4.35	
Vested	(894,988)	3.89	
Restricted share units outstanding at December 31, 2021	<u>2,385,789</u>	<u>4.27</u>	

The total fair value of restricted share units vested during the years ended December 31, 2020 and 2021 was RMB 17,017 and RMB 22,395, respectively. Total compensation cost recognized for the years ended December 31, 2019, 2020 and 2021 was RMB 18,159, RMB 21,280 and RMB 25,711. As of December 31, 2021, there was RMB 51,308 in total unrecognized compensation expense related to such non-vested restricted shares, which is expected to be recognized over a weighted-average period of 2.5 years.

Employee ownership plan of 1 Pharmacy Technology

As disclosed in Note 12, the excess of the fair value of the restricted shares of LLPs issued to the employees of 1 Pharmacy Technology over the issuance price of RMB 32,500 is recognized as share based compensation over the vesting period. The shares issued to the employees in each LLP are not outstanding shares but are restricted with 50% of the shares vesting within two years from the issuance date and the remaining 50% vesting evenly on an annual basis over the 2 years thereafter, which are also subject to adjustment based on performance condition.

For the year ended December 31, 2020, the Group determined the fair value of the restricted shares of LLPs using market approach with the assistance from third party valuation specialist. The fair value of the restricted shares was estimated at RMB 14.19 per share compared with the issuance price of RMB 1.0 per share.

For the year ended December 31, 2021, the Group determined the fair value of the restricted shares using income approach with the assistance from third party valuation specialist. The fair value of the restricted shares was estimated at RMB 13.5 to 14.2 per share compared with the issuance price of RMB 1.0 per share.

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15. SHARE-BASED COMPENSATION (Continued)

The following table summarized the Group's restricted shares of LLPs activities in 2020 and 2021.

	Number of Restricted Share Units of LLPs	Weighted Average Grant Date Fair Value RMB	Weighted average remaining contractual term	Aggregate intrinsic value
Non-vested restricted shares outstanding at January 1, 2020	—	—	—	—
Granted	32,500,000	14.19		
Forfeited	—	—		
Vested	—	—		
Non-vested restricted shares outstanding at December 31, 2020	32,500,000	14.19	3.84	428,675
Granted	5,298,506	13.74		
Forfeited	(6,150,869)	14.17		
Vested	—	—		
Non-vested restricted shares outstanding at December 31, 2021	<u>31,647,637</u>	14.12	2.94	395,595

Total compensation cost recognized for the years ended December 31, 2020 and 2021 was RMB 16,642 and RMB 93,649.

As of December 31, 2021, there was RMB 305,009 in total unrecognized compensation expense related to such non-vested restricted shares, which is expected to be recognized over a weighted-average period of 2.9 years.

Share-based compensation for all share options, restricted share units and employee ownership plan of 1 Pharmacy Technology

The Group recorded share based compensation expense of RMB 54,281, RMB 75,695 and RMB 145,593 for the years ended December 31, 2019, 2020 and 2021, respectively, which were classified in the accompanying consolidated statements of operations as follows:

	Year Ended December 31,		
	2019 RMB	2020 RMB	2021 RMB
General and administrative expenses	25,412	22,727	69,718
Selling and marketing expenses	24,772	40,562	50,532
Technology expenses	4,097	12,406	25,343
Total	<u>54,281</u>	<u>75,695</u>	<u>145,593</u>

As of December 31, 2021, there was RMB 363,230 of total unrecognized compensation expense related to unvested share options, restricted share units and restricted shares of LLPs. That cost is expected to be recognized over a weighted-average period of 2.8 years.

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16. LOSS PER SHARE

The following table sets forth the computation of basic and diluted loss per share for the years indicated:

	Year Ended December 31,		
	2019	2020	2021
Net loss attributable to ordinary shareholders	(499,606)	(456,533)	(669,810)
Weighted average number of ordinary shares-basic and diluted	163,671,577	164,786,631	165,866,901
Net loss per ordinary share-basic and diluted	<u>(3.05)</u>	<u>(2.77)</u>	<u>(4.04)</u>

As a result of the Group's net loss for the three years ended December 31, 2019, 2020 and 2021, share options and restricted share units outstanding in the respective periods were excluded from the calculation of diluted loss per share as their inclusion would have been anti-dilutive.

	As of December 31,		
	2019	2020	2021
Share options and restricted share units	9,311,906	9,436,372	8,312,535

17. INCOME TAX EXPENSE***Cayman Islands***

Under the current laws of the Cayman Islands, the Company is not subject to tax on income or capital gain.

Hong Kong

Yao Wang is subject to Hong Kong profit tax at a rate of 16.5%. No Hong Kong profit tax has been provided as the Group has not had assessable profit that was earned in or derived from Hong Kong during the years presented.

PRC

Under the Law of the People's Republic of China on Enterprise Income Tax ("EIT Law"), domestically-owned enterprises and foreign-invested enterprises are subject to a uniform tax rate of 25%. High-technology enterprises may obtain a preferential tax rate of 15% provided they meet the related criteria. In December 2019, 1 Pharmacy Technology received approval from relevant government authorities to be classified as a "High and New Technology Enterprise" ("HNTE") and 1 Pharmacy Technology is still on the position of loss. The HNTE qualification is valid for three years through 2021.

There is no provision for income taxes because the Company and all of its owned subsidiaries are in cumulative loss positions for all the periods presented.

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17. INCOME TAX EXPENSE (Continued)

PRC (Continued)

A reconciliation between the effective income tax rate and the PRC statutory income tax rate is as follows:

	Year Ended December 31,	
	2020	2021
PRC statutory tax rate	25 %	25 %
Tax effect of other expenses that are not deductible in determining taxable profit	(3)%	(2)%
Tax effect of inter group loan waiver	(35)%	—
Effect of enacted tax rate change	6 %	2 %
Effect of change in valuation allowance	7 %	(25)%
Effective tax rate	<u>0 %</u>	<u>0 %</u>

The principal components of the Group's deferred income tax assets and liabilities as of December 31, 2020 and 2021 are as follows:

	As of December 31,	
	2020	2021
Deferred tax assets:		
Net loss carryforward	286,356	589,792
Advertising expense carried forward for future deduction	30,827	19,123
Accrued expenses and payroll payable	12,594	15,327
Provision for impairment of assets	7,072	6,614
Others	781	361
Valuation allowance	<u>(337,630)</u>	<u>(631,217)</u>
Total deferred tax assets	<u>—</u>	<u>—</u>
Deferred tax liabilities:		
Total deferred tax liabilities	<u>—</u>	<u>—</u>

As of December 31, 2020 and 2021, valuation allowance of RMB 337,630 and RMB 631,217 was provided, respectively. The Group considers positive and negative evidence to determine whether some portion or all of the deferred tax assets will more likely than not be realized. This assessment considers, among other matters, the nature, frequency and severity of recent losses, forecasts of future profitability, the duration of statutory carryforward periods, the Group's experience with tax attributes expiring unused and tax planning alternatives. Valuation allowances have been established for deferred tax assets based on a more likely than not threshold. The Group's ability to realize deferred tax assets depends on its ability to generate sufficient taxable income within the carryforward periods provided for in the tax law.

As of December 31, 2021, the Group had tax loss carryforwards of RMB 2,359,167 which will expire between 2022 and 2031 if not used.

The Group determines whether or not a tax position is "more-likely-than-not" of being sustained upon audit based solely on the technical merits of the position. The Group does not anticipate any significant changes to its liability for unrecognized tax benefits within the next 12 months.

According to the PRC Tax Administration and Collection Law, the statute of limitations is three years if the underpayment of income taxes is due to computational errors made by the taxpayer. The statute of limitations will be extended to five years under special circumstances, which are not clearly defined, but an underpayment of income tax liability exceeding RMB100 is specifically listed as a special circumstance. In the case of a transfer pricing related adjustment, the statute of limitations is ten years. There is no statute of limitations in the case of tax evasion. From 2017 to 2021, the Group's PRC subsidiaries were still within the examination period of the PRC tax authorities.

[Table of Contents](#)**111, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2019, 2020 and 2021****(Amounts in thousands, except for share data and per share data, unless otherwise stated)****17. INCOME TAX EXPENSE (Continued)*****PRC (Continued)***

A deferred tax liability should be recognized for the undistributed profits of the PRC subsidiaries unless the Company has sufficient evidence to demonstrate that the undistributed dividends will be reinvested and the remittance of the dividends will be postponed indefinitely. The Company plans to indefinitely reinvest undistributed profits earned from its PRC subsidiaries in its operations in the PRC. Therefore, no withholding income taxes for undistributed profits of the Company's subsidiaries were provided as of December 31, 2020 and 2021.

18. RELATED PARTY TRANSACTIONS

There were no transaction balances with related parties as of December 31, 2020 and 2021.

There were no related party transactions for the years ended December 31, 2019, 2020 and 2021.

19. MAINLAND CHINA CONTRIBUTION PLAN

Full time employees of the Group in the PRC participate in a government-mandated defined contribution plan pursuant to which certain pension benefits, medical care, unemployment insurance, employee housing fund and other welfare benefits are provided to employees. PRC labor regulations require the Group to accrue for these benefits based on a certain percentage of the employees' salaries. The total contribution for such employee benefits were RMB50,046, RMB28,044 and RMB81,468 for the years ended December 31, 2019, 2020 and 2021, respectively. The Group has no ongoing obligation to its employees subsequent to its contributions to the PRC plan.

20. RESTRICTED NET ASSETS

Pursuant to laws applicable to entities incorporated in the PRC, the subsidiaries of the Group in the PRC must make appropriations from after-tax profit to non-distributable reserve funds. These reserve funds include one or more of the following: (i) a general reserve, (ii) an enterprise expansion fund and (iii) a staff bonus and welfare fund. Subject to certain cumulative limits, the general reserve fund requires annual appropriation of 10% of after tax profit (as determined under accounting principles generally accepted in the PRC at each year-end) until the accumulative amount of such reserve fund reaches 50% of their registered capital; the other fund appropriations are at the subsidiaries' discretion. These reserve funds can only be used for the specific purposes of offsetting future losses, enterprise expansion and staff bonus and welfare and are not distributable as cash dividends. During the years ended December 31, 2019, 2020 and 2021, no appropriation to statutory reserves was made because the PRC subsidiaries had substantial losses during such periods. In addition, due to restrictions on the distribution of share capital from the Company's PRC subsidiaries and VIEs, the PRC subsidiaries and VIEs' share capital and restricted cash of RMB 984,959 and RMB 717,322 at December 31, 2020 and 2021 is considered restricted, which are not available for distribution to the Company by its PRC subsidiaries in the form of dividends, loans or advances.

21. COMMITMENTS AND CONTINGENCIES

The Group is subject to periodic legal or administrative proceedings in the ordinary course of its business. The Group does not believe that any currently pending legal or administrative proceeding to which the Group is a party will have a material adverse effect on the financial statements.

22. SUBSEQUENT EVENTS

In February 2022, the Group terminated the contractual arrangements between 1 Pharmacy Technology and each of the Company's variable interest entities, namely Yihao Pharmacy, Yihao Pharmaceutical and Shanghai Yaowang as well as their respective shareholders, and 1 Pharmacy Technology entered into a share transfer agreement with the former shareholders of the VIE entities. As a result, the Company currently has direct equity control of these entities.

ADDITIONAL FINANCIAL INFORMATION - FINANCIAL STATEMENTS SCHEDULE I
111, INC.

FINANCIAL INFORMATION FOR PARENT COMPANY

CONDENSED BALANCE SHEETS

(Amounts in thousands, except for share data and per share data, unless otherwise stated)

	2020 RMB	2021 RMB	2021 US\$ (Note 2 (ai))
ASSETS			
Current assets:			
Cash and cash equivalents	14,696	12,943	2,031
Short term investments	—	32,156	5,046
Prepayments and other current assets	355,942	4,291	674
Total current assets	<u>370,638</u>	<u>49,390</u>	<u>7,751</u>
Total assets	<u>370,638</u>	<u>49,390</u>	<u>7,751</u>
LIABILITIES AND EQUITY			
Other current liabilities	9,497	51,306	8,051
Deficit of investments in subsidiaries and consolidated VIEs	—	169,868	26,656
Other non-current liabilities	3,736	1,537	241
Total liabilities	<u>13,233</u>	<u>222,711</u>	<u>34,948</u>
SHAREHOLDERS' EQUITY (DEFICIT)			
Ordinary shares Class A (\$0.00005 par value per share; 800,000,000 shares authorized, 96,588,106 shares issued and 93,353,402 and 94,148,486 outstanding as of December 31, 2020 and 2021, respectively)	30	31	5
Ordinary shares Class B (\$0.00005 par value per share; 72,000,000 shares authorized, 72,000,000 shares issued and outstanding as of December 31, 2020 and 2021)	25	25	4
Treasury shares (1,997,620 and 2,330,620 shares as of December 31 2020 and 2021)	(34,972)	(40,859)	(6,412)
Additional paid-in capital	2,669,279	2,817,789	442,173
Accumulated deficit	(2,339,868)	(3,009,678)	(472,284)
Accumulated other comprehensive income	62,911	59,371	9,317
Total shareholders' equity (deficit)	<u>357,405</u>	<u>(173,321)</u>	<u>(27,197)</u>
Total liabilities and shareholders' equity (deficit)	<u>370,638</u>	<u>49,390</u>	<u>7,751</u>

ADDITIONAL FINANCIAL INFORMATION - FINANCIAL STATEMENTS SCHEDULE I
111, INC.

FINANCIAL INFORMATION FOR PARENT COMPANY

CONDENSED STATEMENTS OF COMPREHENSIVE LOSS
(Amounts in thousands, unless otherwise stated)

	Years Ended December 31,			
	2019 RMB	2020 RMB	2021 RMB	2021 US\$ (Note 2 (ai))
Operating expenses:				
General and administrative expenses	(8,523)	(14,202)	(12,141)	(1,905)
Interest income	593	166	26	4
Other operating income, net	—	—	50	8
Other income, net	<u>7,161</u>	<u>2,199</u>	<u>7,089</u>	<u>1,112</u>
Loss before tax and loss from investment in subsidiaries and VIEs	(769)	(11,837)	(4,976)	(781)
Share of loss of subsidiaries and VIEs	(498,837)	(444,696)	(664,834)	(104,327)
Net loss attributable to ordinary shareholders	<u>(499,606)</u>	<u>(456,533)</u>	<u>(669,810)</u>	<u>(105,108)</u>
Other comprehensive income (loss) (net of tax of nil)				
Unrealized securities holding gains	3,356	—	278	43
Realized securities holding gains	(4,962)	—	—	—
Foreign currency translation adjustments	11,668	(13,697)	(4,051)	(635)
Unrealized securities holding gains of subsidiaries and VIEs	3,979	1,137	8,034	1,261
Realized securities holding gains of subsidiaries and VIEs	(4,673)	(970)	(7,801)	(1,224)
Comprehensive loss	<u>(490,238)</u>	<u>(470,063)</u>	<u>(673,350)</u>	<u>(105,663)</u>

ADDITIONAL FINANCIAL INFORMATION - FINANCIAL STATEMENTS SCHEDULE I
111, INC.

FINANCIAL INFORMATION FOR PARENT COMPANY

CONDENSED STATEMENTS OF CASH FLOWS
(Amounts in thousands, unless otherwise stated)

	Years Ended December 31,			
	2019 RMB	2020 RMB	2021 RMB	2021 US\$ (Note 2 (ai))
Operating activities:				
Net loss	(499,606)	(456,533)	(669,810)	(105,108)
Adjustments to reconcile net income to net cash provided by (used in) operating activities:				
Share of loss of subsidiaries and VIEs	498,837	444,696	664,834	104,327
Other current liabilities	43	7,170	(128)	(20)
Other non-current liabilities	(2,199)	(2,200)	(2,199)	(345)
Investment income	(4,962)	—	—	—
Net cash used in operating activities	<u>(7,887)</u>	<u>(6,867)</u>	<u>(7,303)</u>	<u>(1,146)</u>
Investing activities:				
Payment for shareholder loan to subsidiaries	(203,388)	(135,254)	—	—
Purchase of short-term investments	—	—	(32,427)	(5,089)
Proceeds from sale or maturity of short-term investments	117,214	—	—	—
Net cash used in investing activities	<u>(86,174)</u>	<u>(135,254)</u>	<u>(32,427)</u>	<u>(5,089)</u>
Financing activities:				
Proceeds from ordinary shareholders	11,328	6,327	2,918	458
Proceeds from loan from subsidiaries	—	—	41,937	6,581
Payment of share repurchase	(22,991)	(11,981)	(5,887)	(924)
Net cash (used in) provided by financing activities	<u>(11,663)</u>	<u>(5,654)</u>	<u>38,968</u>	<u>6,115</u>
Effect of exchange rate changes on cash and cash equivalents, and restricted cash	18,866	(13,530)	(991)	(155)
Net decrease in cash and cash equivalents	(86,858)	(161,305)	(1,753)	(275)
Cash and cash equivalents at the beginning of the year	262,859	176,001	14,696	2,306
Cash and cash equivalents at the end of the year	<u>176,001</u>	<u>14,696</u>	<u>12,943</u>	<u>2,031</u>

ADDITIONAL FINANCIAL INFORMATION - FINANCIAL STATEMENTS SCHEDULE I
111, INC.

FINANCIAL INFORMATION FOR PARENT COMPANY

Note to Schedule I

Schedule I has been provided pursuant to the requirements of Rule 12-04(a) and 5-04-(c) of Regulation S-X, which require condensed financial information as to the financial position, change in financial position and results of operations of a parent company as of the same dates and for the same periods for which audited financial statements have been presented when the restricted net assets of consolidated subsidiaries exceed 25 percent of consolidated net assets as of the end of the most recently completed fiscal year.

The condensed financial information has been prepared using the same accounting policies as set out in the consolidated financial statements except that the equity method has been used to account for investments in its subsidiaries and consolidated VIEs. For the parent company, the Group records its investments in subsidiaries and consolidated VIEs under the equity method of accounting as prescribed in ASC 323, Investments—Equity Method and Joint Ventures. Such investments are presented on the Condensed Balance Sheets as “Deficit of investments in subsidiaries and consolidated VIEs” and the subsidiaries and consolidated VIEs’ losses as “Share of loss of subsidiaries and VIEs” on the Condensed Statements of Comprehensive Loss. Ordinarily under the equity method, an investor in an equity method investee would cease to recognize its share of the losses of an investee once the carrying value of the investment has been reduced to nil absent an undertaking by the investor to provide continuing support and fund losses. For the purpose of Schedule I, the parent company has continued to reflect its share, based on its proportionate interest, the losses of subsidiaries and consolidated VIEs regardless of the carrying value of the investment even though the parent company is not obligated to provide continuing support or fund losses.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. The footnote disclosures contain supplemental information relating to the operations of the Company and, as such, these statements should be read in conjunction with the notes to the accompanying financial statements.

As of December 31, 2021, there are no material contingencies, mandatory dividend and significant provisions for long-term obligations or guarantees of the Company, except for those which have separately disclosed in the financial statements.

List of Significant Subsidiaries of the Registrant

Name of Subsidiary	Jurisdiction of Incorporation
Yao Wang Corporation Limited	Hong Kong
1 Pharmacy Technology (Shanghai) Co., Ltd.	PRC
Chongqing Yihao Pharmacy Co., Ltd.	PRC
Wuhan Central China Drug Trading Co., Ltd.	PRC
Fujian Yaofang Pharmacy Co., Ltd.	PRC
Hubei Yihao Pharmacy Co., Ltd.	PRC
Liaoning Yihao Pharmacy Co., Ltd.	PRC
Shanxi Yihao Yaofang Pharmacy Co., Ltd.	PRC
Tianjin Yihao Pharmacy Co., Ltd.	PRC
Guangdong Yihao Pharmacy Co., Ltd.	PRC
Guangdong Yihao Pharmaceutical Chain Co., Ltd.	PRC
Shanghai Yaowang E-Commerce Co., Ltd.	PRC
Chengdu Yizhen Internet Hospital Co., Ltd.	PRC
Kunshan Yihua Hospital Co., Ltd.	PRC
Kunshan Yifang Pharmacy Co., Ltd.	PRC
Yijianyikang Medical Technology (Shanghai) Co., Ltd.	PRC

**Certification by the Principal Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Junling Liu, certify that:

1. I have reviewed this annual report on Form 20-F of 111, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;

4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

(c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and

5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: April 29, 2022

By: /s/ Junling Liu

Name: Junling Liu

Title: Chief Executive Officer

**Certification by the Principal Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Junling Liu, certify that:

1. I have reviewed this annual report on Form 20-F of 111, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;

4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

(c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and

5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: April 29, 2022

By: /s/ Junling Liu

Name: Junling Liu

Title: Chief Executive Officer, acting in the capacity of Chief
Financial Officer

**Certification by the Principal Executive Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the Annual Report of 111, Inc. (the “Company”) on Form 20-F for the year ended December 31, 2021 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Junling Liu, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: April 29, 2022

By: /s/ Junling Liu
Name: Junling Liu
Title: Chief Executive Officer

**Certification by the Principal Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the Annual Report of 111, Inc. (the “Company”) on Form 20-F for the year ended December 31, 2021 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Junling Liu, acting in the capacity of Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: April 29, 2022

By: /s/ Junling Liu
Name: Junling Liu

Title: Chief Executive Officer, acting in the capacity of Chief Financial Officer

Our ref KKZ/742474-000001/19339623v1

111, Inc.
3-5/F, No.295 ZuChongZhi Road,
Pudong New Area
Shanghai, 201203
The People's Republic of China

April 29, 2022

Dear Sir and/or Madam

111, Inc.

We have acted as legal advisers as to the laws of the Cayman Islands to 111, Inc., an exempted limited liability company incorporated in the Cayman Islands (the “**Company**”), in connection with the filing by the Company with the United States Securities and Exchange Commission (the “**SEC**”) of an annual report on Form 20-F for the year ended 31 December 2021 (the “**Annual Report**”).

We hereby consent to the reference to our firm under the headings “Item 10. Additional Information—B. Memorandum and Articles of Association” and “Item 10. Additional Information—E. Taxation—Cayman Islands Taxation” in the Annual Report, and we further consent to the incorporation by reference of the summary of our opinions under these headings into the Company’s registration statement on Form S-8 (File No. 333-229313) that was filed on 22 January 2019, pertaining to the Company’s 2013 Share Incentive Policy, 2014 Share Incentive Policy, 2016 Share Incentive Plan and 2018 Share Incentive Plan.

We consent to the filing with the SEC of this consent letter as an exhibit to the Annual Report. In giving such consent, we do not thereby admit that we come within the category of persons whose consent is required under Section 7 of the Securities Act of 1933, or under the Securities Exchange Act of 1934, in each case, as amended, or the regulations promulgated thereunder.

Yours faithfully

/s/ Maples and Calder (Hong Kong) LLP

**CONSENT OF INDEPENDENT REGISTERED PUBLIC
ACCOUNTING FIRM**

We consent to the incorporation by reference in Registration Statement No. 333-229313 on Form S-8 of our reports dated April 29, 2022, relating to the financial statements of 111, Inc. and the effectiveness of 111, Inc.'s internal control over financial reporting appearing in this Annual Report on Form 20-F for the year ended December 31, 2021.

/s/ Deloitte Touche Tohmatsu Certified Public Accountants LLP

Shanghai, China

April 29, 2022
