

## STATEMENT OF DISCIPLINARY ACTION

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### Exchange's Disciplinary Action against China Fortune Investments (Holding) Limited (Stock Code: 8116) and Nine Directors

**Directors must devote sufficient time and attention to, and take an active interest in, the affairs of the listed issuer, including implementing adequate supervisory and monitoring mechanisms over the affairs of its subsidiaries. Failure to do so falls short of the standards expected of directors of listed companies and amounts to a dereliction of their duties.**

**Breaches of duty by directors are viewed seriously by the Exchange. Where failures are established, directors can expect both disciplinary sanctions to be imposed and that their breaches will be taken into account in the Exchange's assessment of their suitability to be appointed directors of issuers listed or to be listed on the Exchange.**

### The GEM Listing Committee of The Stock Exchange of Hong Kong Limited (GEM Listing Committee)

#### CENSURES:

(1) **China Fortune Investments (Holding) Limited** (Stock Code: 8116) (**Company**)

for failing to publish and announce in a timely manner four sets of financial results and reports in breach of Rules 18.03, 18.48A, 18.49, 18.50C, 18.53, 18.54, 18.66, 18.67, 18.78, and 18.79 of the Rules Governing the Listing of Securities on GEM of The Stock Exchange of Hong Kong Limited (**GLR**); and failing to announce two disclosable transactions in a timely manner in breach of GLR 19.34; and

(2) **Mr Xu Jing An (Mr Xu)**, independent non-executive director (**INED**) of the Company;

(3) **Ms Li Ka Ki (Ms Li)**, former executive director (**ED**) of the Company; and

(4) **Ms Ching Wai Han (Ms Ching)**, former INED of the Company

for failing to exercise care, skill and diligence required of them as directors of the Company in breach of GLR 5.01(6) and their obligations under the Director's Declaration and Undertaking given to the Exchange in the form set out in Appendix 6A of the GLR (**Undertaking**) to comply with the GLR to the best of their abilities by failing to put in place adequate internal controls systems,

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**AND FURTHER CENSURES:**

- (5) **Mr Stephen William Frostick (Mr Frostick)**, ED of the Company; and
- (6) **Mr Liu Yun Ming (Mr Liu)**, former ED of the Company

for failing to discharge their obligations under GLR 5.01(6) and the Undertakings to comply with the GLR to the best of their abilities by failing to put in place adequate internal controls systems, and failing to cooperate in the Listing Division (**Division**)'s investigation.

**And the Listing Review Committee (LRC) on review****CRITICISES:**

- (7) Mr Cheng Chun Tak (**Mr Cheng**), ED and former Chairman of the Company;
- (8) Mr Huang Sheng Lan (**Mr Huang**), non-executive director of the Company;
- (9) Mr Chang Jun (**Mr Chang**), INED of the Company; and
- (10) Mr Lee Chi Hwa Joshua (**Mr Lee**), former INED of the Company.

(The directors identified at (7) to (10) above are collectively referred to as the **Reviewing Directors**)

(The directors identified at (2) to (10) above are collectively referred to as the **Relevant Directors**).

**HEARINGS**

On 24 November 2020, the GEM Listing Committee conducted a hearing into the conduct of the Company and the Relevant Directors in relation to their obligations under the GLR and the Undertakings.

On 17 May 2021, the LRC conducted a hearing of the review application of the Reviewing Directors with respect to the findings of breaches and sanctions imposed by the GEM Listing Committee.

**FACTS**

The Company was principally engaged in (a) retail and wholesale of wine, cigar, golf products, and trading of watches and jewelries; and (b) a P2P Business carried out by the Company's subsidiary acquired in November 2017 (**Acquisition**), Koudai Network Services Company Limited (**Subsidiary**) in the PRC. Fraud was found to have been perpetrated by the directors and senior management of the Subsidiary to defraud the Subsidiary as well as the Company before and after the Acquisition.

Between 14 November 2018 and 14 August 2019, the Company failed to publish four sets of financial results and reports as they fell due under the GLR as follows (**Late Publications**):

	Publications	Period end	Due date	Publication date	Delay (approx.)	Relevant Listing Rules
1	3Q2018 Results/Report	nine months ended 30 September 2018	14 November 2018	3 November 2019	11.5 months	GLR 18.66, 18.67, & 18.79
2	FY2018 Results/Report (disclaimer of opinion)	year ended 31 December 2018	31 March 2019	3 November 2019	7 months	GLR 18.03, 18.48A, 18.49 & 18.50C
3	1Q2019 Results/Report	three months ended 31 March 2019	15 May 2019	3 November 2019	5.5 months	GLR 18.66, 18.67 & 18.79
4	1H2019 Results/Report	six months ended 30 June 2019	14 August 2019	3 November 2019	2.5 months	GLR 18.53, 18.54 & 18.78

The delays resulted in a suspension of trading in the Company's shares for over two years from 5 November 2018.

In addition, the Company entered into two agreements on 22 September 2018 and 9 October 2018 to dispose of certain properties of the Subsidiary in Chengdu and Shenzhen (**Disposals**). The Disposals were not announced until 16 October 2018 and 16 November 2018, respectively.

Further, there were two loan agreements entered into between the Subsidiary and independent third parties in May 2018 without the prior knowledge and authorization of the Company (**Loan Transactions**). The loans under the Loan Transactions were not recorded in the Company's books and records.

## EXCHANGE LISTING RULE REQUIREMENTS

Under GLR 19.34, a listed issuer is required to publish an announcement of the terms of, among others, a disclosable transaction as soon as possible.

The GLR requirements in relation to financial reporting are as follows:

- (a) GLR 18.03, 18.48A, 18.49, and 18.50C require a listed issuer to announce and publish its annual results and annual reports in respect of a financial year no later than three months after the end of the reporting year;
- (b) GLR 18.53, 18.54, and 18.78 require a listed issuer to announce and publish its half-year results and reports for each of the first 6 months of each financial year no later than 45 days after the end of such period; and
- (c) GLR 18.66, 18.67 and 18.79 require a listed issuer to announce and publish its quarterly results and reports for each of the first 3 and 9 month periods of each financial year no later than 45 days after the end of such period.

Under GLR 5.01 and 5.03, the board of directors of an issuer is collectively responsible for its management and operations, and the directors are collectively and individually responsible for the issuer's compliance with the GLR.

GLR 5.01 provides that the Exchange expects directors of an issuer, both collectively and individually, to fulfil fiduciary duties and duties of skill, care and diligence to a standard at least commensurate with the standard established by Hong Kong law. Specifically, they should “*apply such degree of skill, care and diligence as may reasonably be expected of a person of his knowledge and experience and holding his office within the issuer*”. Further, while delegating their functions is permissible, “*they must take an active interest in the issuer's affairs and obtain a general understanding of its business.*”

Each of the Relevant Directors has given the Undertaking in the form of Appendix 6A of the GLR, which provides, among others, that directors shall:

- (a) comply to the best of their ability with the GLR;
- (b) cooperate in any investigation conducted by the Division, including answering promptly and openly any questions addressed to them and promptly producing the originals or copies of any relevant documents; and
- (c) inform the Exchange of any change to their contact details for correspondence from and service of notices and other documents by the Exchange, for a period of 3 years from the date on which they cease to be directors of the issuer.

## **FINDINGS OF BREACH**

The GEM Listing Committee (and the LRC with respect to the Reviewing Directors) considered the written and oral submissions of the Division and the Relevant Directors and concluded as follows:

### **Company's breaches**

Given the delay in the Company's publication of four sets of financial results and reports, the Company repeatedly breached GLR18.03, 18.48A, 18.49, 18.50C, 18.53, 18.54, 18.66, 18.67, 18.78, and 18.79.

The Company admitted its breach of GLR 19.34 in respect of the disclosure of the Disposals.

### **Internal controls deficiencies**

There was a lack of adequate and effective internal controls in relation to the operations and affairs of the Subsidiary by the Company which had led to the Disposals and Loan Transactions being carried out in an unauthorized manner and undetected and which ultimately also led to the Late Publications.

**Relevant Directors' breaches**

The Relevant Directors, individually and collectively, failed to demonstrate the exercise of skill, care and diligence required and expected from them under GLR 5.01(6). Amongst other things:

- (a) there were no policies or procedures in place providing adequate oversight of the Subsidiary, including custody and control over the use of the Subsidiary's official seals and business license, including keeping proper records of each use thereof;
- (b) the Relevant Directors did not appear to have taken any concrete step towards ensuring that the Company had adequate internal controls in relation to the operations and affairs of the Subsidiary in place, in particular integration of the Subsidiary into the Company's internal controls after the Acquisition;
- (c) the Relevant Directors did not appear to have conducted any review or discussion of the Company's internal controls in relation to the operations and affairs of the Subsidiary; and
- (d) the Relevant Directors did not appear to have (i) a good understanding of what internal controls the Company had in place in relation to the operations and affairs of the Subsidiary; and/or (ii) considered their adequacy or whether any rectification/improvement was required. Although there was an assertion that the audit function had been outsourced, ultimate responsibility for the performance of that function remained with the Relevant Directors.

Based on the above, and by virtue of the Relevant Directors' breaches of GLR 5.01(6), the GEM Listing Committee (and the LRC with respect to the Reviewing Directors) further concluded that each of the Relevant Directors also breached their Undertakings to comply with the GLR to the best of his/her ability by failing to put in place adequate internal controls systems during the period between May 2018 and October 2018.

**Breach of the Undertaking to cooperate with the Division's Investigation**

In the course of the Division's investigation, enquiries were made with Mr Frostick through the Company and Mr Liu at their last known address. Mr Frostick informed the Division that he disagreed with certain submissions made by the Company. However, he did not submit his own submission in reply as requested and required. Mr Liu provided the Division with his latest correspondence address during the investigation, but then failed to reply to the Division's enquiries, and did not make any submissions.

The GEM Listing Committee accordingly concluded that Mr Frostick and Mr Liu breached their Undertakings to cooperate in the Division's investigation.

**REGULATORY CONCERNS**

The GEM Listing Committee regarded the breaches in this matter as serious:

- (1) The GLR are designed to ensure that investors have a continued confidence in the market and that they are kept fully informed by the Company. In this regard, it is important that issuers publish their financial information in accordance with the timeframe under the GLR.
- (2) This case is a reminder of the role that directors must play to ensure a listed issuer's compliance with the GLR. The Relevant Directors' conduct fell short of proper corporate governance practice. No systemic internal controls were implemented for the newly acquired business carried out by the Subsidiary. It was clear that the Company did not have sufficient oversight in the operations and affairs of the Subsidiary at the relevant time, which increased the risks of unauthorized transactions entered into by the Subsidiary's employees, and ultimately led to the Disposals, the Loan Transactions and the Late Publications. The deficiencies in this respect prevented the Company's auditors from expressing an opinion on the consolidated financial statements of the Company, which was relevant to the assessment of the Company by the shareholders and the public, and a loss of approximately \$288 million was resulted for the Company in FY2018.
- (3) It is important that the issuer's board of directors takes seriously its obligations to review the issuer's internal controls and risk management system (including that in relation to the operations and affairs of its subsidiaries) and to follow up on any matters or deficiencies identified. The review must be made on an ongoing basis to ensure it is adequate and effective, and should also cover all the material aspects, including financial, operational and compliance controls.
- (4) A director's compliance with his/her obligations in the Undertaking is of utmost importance in enabling the Exchange to discharge its function to ensure so far as reasonably practicable, an orderly, informed and fair market in securities that are traded on the Exchange.

The GEM Listing Committee (and the LRC with respect to the Reviewing Directors) noted from the Company's announcement in October 2019 that the internal controls consultant conducted a follow-up review and confirmed that the Company had implemented remedial measures to address all the internal controls deficiencies identified. The remedial measures taken reflected the inadequacy of the Company's internal controls at the material time.

## **SANCTIONS**

Having made the findings of breaches stated above, and having concluded that the breaches were serious, the GEM Listing Committee (and the LRC with respect to the Reviewing Directors) decided to:

- (1) censure the Company for breaching GLR 18.03, 18.48A, 18.49, 18.50C, 18.53, 18.54, 18.66, 18.67, 18.78, 18.79 and 19.34;

- (2) censure each of Mr Xu, Ms Li and Ms Ching for breaching GLR 5.01(6) and their Undertakings to comply with the GLR to the best of their abilities;
- (3) further censure each of Mr Frostick and Mr Liu for breaching GLR 5.01(6) and their Undertakings to comply with the GLR to the best of their abilities and to cooperate with the Division's investigation; and
- (4) criticize each of Mr Cheng, Mr Huang, Mr Lee and Mr Chang for breaching GLR 5.01(6) and their Undertakings to comply with the GLR to the best of their abilities.

The GEM Listing Committee (and the LRC with respect to the Reviewing Directors) further directed:

- (1) each of Mr Cheng, Mr Frostick, Mr Huang, Mr Lee, Mr Chang and Mr Xu (current directors of issuers) to (a) attend 20 hours of training on Listing Rule compliance, including at least three hours on each of (i) directors' duties and (ii) the Listing Rule requirements for corporate governance and internal controls (**Training**), to be provided by training providers approved by the Division and completed within 90 days from the publication of this Statement of Disciplinary Action; and (b) provide the Division with the Training provider's written certification of full compliance within two weeks after Training completion;
- (2) as a pre-requisite of any future appointment as a director of any company listed or to be listed on the Exchange, Mr Liu, Ms Li and Ms Ching (former directors) to attend 20 hours of the Training, to be provided by training providers approved by the Division. The Training is to be completed, and the Training provider's written certification of full compliance is to be provided to the Division, before the effective date of any such appointment;
- (3) the Company to publish an announcement to confirm that the direction in paragraph (1) above has been fully complied with within two weeks after the fulfilment of such direction;
- (4) the Company to submit drafts of the announcement referred to in paragraph (3) above for the Division's comment and may only publish the announcement after the Division has confirmed it has no further comment on it; and
- (5) following the publication of this Statement of Disciplinary Action, any changes necessary and any administrative matters which may emerge in the management and operation of any of the directions set out in paragraphs (1) to (4) above to be directed to the Division for consideration and approval. The Division should refer any matters of concern to the Committee for determination.

For the avoidance of doubt, the Exchange confirms that the sanctions and directions in this Statement of Disciplinary Action apply only to the Company and the Relevant Directors, and not to any other past or present members of the board of directors or supervisors of the Company.

Hong Kong, 7 July 2021