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中滔環保

**CT ENVIRONMENTAL GROUP LIMITED**  
**中滔環保集團有限公司**

*(Incorporated in the Cayman Islands with limited liability)*

**(Stock Code: 1363)**

**SUPPLEMENTAL ANNOUNCEMENT**  
**IN RELATION TO THE ANNUAL RESULTS ANNOUNCEMENT**  
**AND THE ANNUAL REPORT**  
**FOR THE YEAR ENDED 31 DECEMBER 2017**

References are made to the annual results announcement for the year ended 31 December 2017 (the “**Results Announcement**”) of CT Environmental Group Limited (the “**Company**”) dated 29 March 2018 and the annual report 2017 of the Company (the “**Annual Report**”).

The board of directors of the Company (the “**Board**”) wishes to provide the following information which is supplemental to the Results Announcement and the Annual Report. Unless otherwise defined, capitalized terms used in this announcement shall have the same meanings as in the Results Announcement.

## **BASIS FOR QUALIFIED OPINION**

As stated in the Results Announcement, the then auditors of the Company, KPMG (the “**Previous Auditors**”), requested the management of the Company to provide explanations and supporting documents to substantiate and ascertain the validity of the underlying transactions in relation to the turnover amounting to HKD61.6 million recorded in the provision of sludge and solid waste treatment services business segment of the Group (the “**Transactions**”). The Transactions were in relation to the provision of solid wastes treatment services by the Group to ten customers (the “**Relevant Customers**”) for the year ended 31 December 2017.

## **THE RELEVANT CUSTOMERS**

To the best of the knowledge, information and belief of the Directors, each of the Relevant Customers were third parties independent of the Company and connected persons of the Company, and each of the Relevant Customers were independent of each other.

## **THE REQUISITIONS OF THE PREVIOUS AUDITORS**

During the course of the audit, the Previous Auditors requested the Company to provide supporting documents in relation to the Transactions including, solid wastes treatment service agreements, value-added tax invoices, solid wastes transportation invoices, weighing lists (過磅單) and other related supporting documents, monthly statement with the Relevant Customers, and fee receipt records. In addition, the Previous Auditors also requested the Company to arrange face to face interviews with the legal representatives and head of finance for each of the Relevant Customers to be conducted at the premises or facilities of those customers, and provide signed acknowledgment of the interviews.

In response to the document requests by the Previous Auditors, the Company provided all requested supporting documents, other than :1) the settlement record of part of the trade receivables arose from the Transactions (which had not been settled yet); 2) certain value-added tax invoices; and 3) the solid wastes transportation invoices. As all transportation of solid wastes from customers to facilities of the Group were arranged by the customers, the Group did not have any solid wastes transportation invoices in their record. Instead, the Company provided the Previous Auditors with the relevant weighing lists of the solid wastes delivered to the Company and the Company regarded that it was an alternative supporting document.

As the requests of the Previous Auditors for face to face interviews with the Relevant Customers were not made until mid of March 2018, and the Relevant Customers were independent third parties to the Company, the Company faced difficulty in arranging interviews with the Relevant Customers in time for the audit.

To the best knowledge of the Company, as the Company was unable to arrange face to face interviews with the Relevant Customers at the customers' premises as requested by the Previous Auditors, the Previous Auditors considered the information provided by the Company as a whole after taking into account the findings (as defined below) were insufficient to substantiate the Transactions, which led to the audit qualification.

## **THE FINDINGS**

During the course of the audit, the Previous Auditors had the following major findings on the characteristic of the Transactions as extracted (and translated from Chinese to English) from the report provided to the audit committee of the Company by the Previous Auditors during the audit committee meeting held for considering the Results Announcement (the "**Findings**") and had required the Company to provide further explanations. Due to time constraint, explanations were not provided by the Company to the Previous Auditors before the publication of the Results Announcement:

- (i) *"The Transactions were from ten Relevant Customers, nine of which were new customers of Qingyuan Lvyou and Longmen Zhongtao Environmental Protection Technology Company Limited ("**Longmen Zhongtao**")"*
- (ii) *"Approximately HKD50 million of the turnover arising from the Transactions were recognized between November 2017 and December 2017"*
- (iii) *"The average service fee charged by Qingyuan Lvyou and Longmen Zhongtao to their respective Relevant Customers under the Transactions were higher than the average service fees charged to the same type of service to other existing customers of the Group."*
- (iv) *"The unit cost of providing the treatment services to the Relevant Customers under the Transactions were far lower than the corresponding unit cost of providing the same type of treatment services to other customers of the Group"*

- (v) *“As of 31 December 2017, the corresponding trade receivables to the Transactions of approximately HKD 72.1 million had not yet been collected”*
- (vi) *“The size of the Transactions between certain Relevant Customers and the Group did not match with the scale of that customer’s operations (in terms of turnover, costs, net profits, assets and liabilities etc.) based on information available from company search.”*
- (vii) *“According to the delivery receipt (收貨單) provided by the Group (which were all hand-written), the sequence of some of the delivery receipt numbers did not match with the date on the delivery receipts chronologically (for example, the delivery date shown on a particular pre-numbered delivery receipts was later than the delivery date shown on another delivery receipts which have an earlier sequence number.)”*
- (viii) *“We were not able to locate the operation site for three of the ten Relevant Customers, the address of which were registered under the Industrial and Commerce Bureau.”*

## **COMPANY’S OBSERVATIONS ON THE FINDINGS**

To the best knowledge of the Directors, the observations to each of the Findings are as follows (save for the observation under Findings (v) in which the Company have provided copies of bank-in slips related to the receipt of approximately RMB15.1 million from the Relevant Customers, all the other observations had not been communicated with the Previous Auditors):

- **Findings (i) and (ii):** Although Qingyuan Lvyou and Longmen Zhongtao provided services to such customers in 2017, six out of nine Relevant Customers were not new to the Group as either Qingyuan Lvyou or Guangzhou Lvyou Industrial Waste Reclamation Treatment Company Limited (“**Guangzhou Lvyou**”, a subsidiary of the Group) had provided services to them occasionally before the Transactions from 2004 to 2014 (notwithstanding that they were not regular customers). Further, it is a market practice that most of the solid wastes collection and recycling companies, being customers of the Group, would accumulate solid wastes to be treated by the end of a calendar year. In addition, Longmen Zhongtao only commenced operations in November 2017. The revenue from its operations therefore only occurred at the end of 2017.

- **Findings (iii):** The services provided by the Group to the Relevant Customers for the Transactions were solid wastes treatment services. Different service fees were charged to the customers based on the types of solid wastes, the complexity of wastes treatment services required, and the level of pollution of the solid wastes. The types of solid wastes ranges from packing scrap wastes (廢包裝邊角料), construction wastes (建築廢渣), packing plastic wastes (廢包裝塑膠), wood shavings wastes (廢木屑) to washing wastes (洗水廢渣) etc..

Most Relevant Customers under the Transactions operated a business of collecting solid wastes, and performing simple classification to extract those wastes with potential resale value. Wastes without resale value were then disposed of by the Relevant Customers in landfill sites catered specifically for general industrial solid wastes. As most local landfills in the vicinity are designed for disposal of municipal solid wastes only, each of Qingyuan Lvyou and Longmen Zhongtao was able to charge the Relevant Customers higher unit prices for treatment services in landfills for general industrial solid wastes operated by them.

- **Findings (iv):** Most of the solid wastes of the Relevant Customers were treated by disposal in solid wastes landfill sites operated by Qingyuan Lvyou and Longmen Zhongtao respectively. The initial capital expenditure in constructing the landfill site is large and the process of obtaining approval in building such landfill sites is lengthy. After the landfill sites commenced operation, other than the fixed cost in relation to the depreciation of the landfills sites, the actual variable costs in relation to the Transactions were low as there is no material variable cost save for certain labor costs in driving the dredge and related fuel costs.
- **Findings (v):** As at the date of the Results Announcement, the Company received RMB17.0 million from the Relevant Customers (representing approximately 27.3% of the trade receivables of the Relevant Customers). Due to time constraint, the Company only provided copies of bank-in slips in relation to an aggregate amount of approximately RMB15.1 million to the Previous Auditors.

- **Findings (vi):** Based on the company search results conducted by the Group in May 2018, no key financial figures were disclosed by seven Relevant Customers, one Relevant Customer was newly incorporated in 2017 and had therefore not filed any financial statements, while the remaining two Relevant Customers disclosed key financial figures but only on a voluntary basis. As the actual basis adopted by the Relevant Customers to derive the disclosed financial figures were not known to the Company, the actual size and scale of the Relevant Customers cannot be accurately inferred from the financial information obtained in the public domain.
  
- **Findings (vii):** Pre-printed delivery receipt booklets (each containing 25 sets of delivery receipts) were purchased directly from third party sellers in bulk. The Group assigned and stored the booklets in different delivery trucks. The actual usage of the pre-printed delivery receipts may therefore not be in sequence as the delivery trucks worked in different customers' location at different times.
  
- **Findings (viii):** As represented by the Relevant Customers, most of them had a registered address (as registered under the Industrial and Commerce Bureau) different from their actual operation site.

## **THE BOARD AND AUDIT COMMITTEE'S VIEW**

The Board and the audit committee of the Company are of the view that the Transactions are properly substantiated and are authentic since the Group had duly entered into written agreements with each of the Relevant Customers with respect to the Transactions, together with other ancillary documents, and the Findings can be explained by the observations as disclosed under the paragraph "Company's Observations on the Findings". Further, the relevant amounts of the Transactions are also fairly stated in the consolidated financial statements as they are consistent with the amounts as stated in the written agreements with each of the Relevant Customers.

## **PLANS TO RESOLVE THE AUDIT QUALIFICATION**

To resolve the audit qualification raised by the Previous Auditors and to prevent the issuance of similar audit qualification by the new auditor of the Company, RSM Hong Kong (“RSM”), the Company has taken and will take the following steps (such steps had not been communicated with the Previous Auditors and the Previous Auditors had not been involved in formulating the plans):

- Since May 2018, the Company has actively reached out to the Relevant Customers regarding the face to face interviews. As at the date of this announcement, all the Relevant Customers have responded that they will, on a best effort basis, assist with the audit procedure. The Company will continue to liaise with the Relevant Customers on the proposed interviews with RSM. It is currently expected that the first customer interview will commence in July 2018 (subject to further confirmation of the interview schedule with the Relevant Customers and RSM).
- The Group will continue to follow up with the Relevant Customers for repayment of the remaining outstanding trade receivables in accordance with the terms of the service contracts. The Company expects that the outstanding trade receivables will be repaid by the Relevant Customers within July 2018.
- The Company shall continue to maintain close communications with RSM, and will use its best efforts to meet their requests for information and/or specific requirements in order to resolve the audit qualification. As at the date of this announcement, the Company had provided certain relevant supporting documents (including a breakdown of the ten customers and respective contracts) to RSM, and RSM will commence preliminary review of relevant documents in order to understand the background of the Transactions and the Relevant Customers as soon as practicable.
- The Company plans to devise internal control procedures on the usage of the pre-numbered delivery receipts by keeping logs on both the used and unused delivery receipts, and will assign a responsible staff to maintain the logs. It is expected that the internal control procedures will be designed by the internal control team of the Company within July 2018.

The Board is of the view, and the audit committee of the Company concurs, that the Previous Auditors' concerns could be addressed by the implementation of the plans set out above and, can therefore prevent similar qualifications by RSM.

On behalf of the Board  
**CT Environmental Group Limited**  
**Tsui Cham To**  
*Chairman*

Hong Kong, 17 July 2018

*As at the date of this announcement, the executive Directors are Mr. Tsui Cham To, Mr. Xu Zhencheng, Mr. Xu Shubiao, Mr. Xu Juwen, the non-executive Director is Mr. Yang Chunlin and the independent non-executive Directors are Mr. Suen To Wai, Mr. Zhang Lu Fu and Mr. Liu Yung Chau.*