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**CHINA FORESTRY HOLDINGS CO., LTD.**

**中國森林控股有限公司**

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

**(Stock Code: 930)**

**ANNOUNCEMENT**

**PROGRESS UPDATE**

**FINDINGS BY THE INDEPENDENT BOARD COMMITTEE**

**AND**

**RECTIFICATION MEASURES TAKEN BY THE COMPANY**

Reference is made to the announcements of the Company dated 26 January 2011, 31 January 2011, 2 March 2011 and 3 March 2011, respectively.

As disclosed in the announcement of the Company dated 31 January 2011, in the course of the audit process in respect of the financial statements for the year ended 31 December 2010, irregularities have been reported by KPMG, the auditors of the Company, to the Board by a letter dated 25 January 2011 and a letter dated 27 January 2011, respectively, subsequent to previous discussions between the Company and KPMG.

In light of the seriousness of the irregularities reported by KPMG, the Company applied for suspension in trading of its Shares from 10:24 a.m. on 26 January 2011.

The Independent Board Committee comprising of Mr. Liu Can, an independent non-executive director, Mr. Zhu Demiao, an independent non-executive director, and Mr. Xiao Feng, a non-executive director, has been formed to conduct an investigation of the matters concerned.

The Board would like to inform the Shareholders and the investment public of the following matters:

- (i) the audit related issues identified by KPMG and other issues identified by the Independent Board Committee;
- (ii) the relevant findings by the Independent Board Committee in respect of these audit related and other issues; and
- (iii) the measures taken by the Company to address these audit related and other issues.
- (iv) the Independent Board Committee is of the view that the Former Management Team was the source of the above irregularities reported by it or KPMG; and
- (v) the dismissal and resignation of the Former Management Team and appointment of the current management team of the Company.

## INTRODUCTION

Reference is made to the announcements (the “**Announcements**”) of China Forestry Holdings Co., Ltd. (the “**Company**”, and together with its subsidiaries, the “**Group**” and each a “**Group Company**”) dated 26 January 2011, 31 January 2011, 2 March 2011 and 3 March 2011, respectively. Unless otherwise stated, terms defined in the Announcements shall have the same meanings when used herein.

As disclosed in the announcement of the Company dated 31 January 2011, in the course of the audit process in respect of the financial statements for the year ended 31 December 2010, irregularities have been reported by KPMG, the auditors of the Company to the Board by a letter dated 25 January 2011 and a letter dated 27 January 2011, respectively, subsequent to previous discussions between the Company and KPMG.

In light of the seriousness of the irregularities reported by KPMG, the Company applied for suspension in trading of its Shares from 10:24 a.m. on 26 January 2011.

An independent board committee (the “**Independent Board Committee**”) comprising of Mr. Liu Can, an independent non-executive director, Mr. Zhu Demiao, an independent non-executive director, and Mr. Xiao Feng, a non-executive director, has been formed to conduct an investigation of the matters concerned.

The Board would like to inform the Shareholders and the investment public of the following matters:

- (i) the audit related issues identified by KPMG and other issues identified by the Independent Board Committee;
- (ii) the relevant findings by the Independent Board Committee in respect of these audit related and other issues; and
- (iii) the measures taken by the Company to address these audit related and other issues.
- (iv) the Independent Board Committee is of the view that the former management team comprising of, among others, Mr. Li Han Chun (the former chief executive officer), Ms. Wu Xiaofen (the former joint chief financial officer), Mr. Zhang Hongyu (the former chief resource officer), Ms. Lv Aoqian (the former chief human resource officer), Mr. Wen Guoping (the former joint chief financial officer) and Mr. Li Haijun (the former the chief sales officer) (together the “**Former Management Team**”) was the source of the above irregularities reported by it or KPMG; and
- (v) the dismissal and resignation of the Former Management Team and appointment of the current management team of the Company.

## **AUDIT RELATED AND OTHER ISSUES**

### **(A) Bank Statements and Bank-in Slips**

#### *(i) Issue*

In the course of the audit process of KPMG, the Former Management Team provided KPMG with copies of (a) bank statements of a Group Company maintained with a PRC commercial bank; and (b) bank-in slips provided by customers of the Group and issued by a PRC commercial bank. KPMG had serious doubt about to the authenticity of such bank statements and bank-in slips.

#### *(ii) Relevant Findings by the Independent Board Committee*

As part of its investigation, the Independent Board Committee obtained bank statements directly from the relevant PRC commercial bank, which indicated that the bank statements and bank-in slips provided by the Former Management Team to KPMG were falsified copies.

In connection with this finding, the Independent Board Committee further discovered that (a) the Group was engaged in certain cash transactions and the sales revenue in respect of which might not have been entirely booked in the accounts of the Group previously presented to

the Board; and (b) sales proceeds in cash generated from the above cash transactions might have been utilized to purchase wood logs. Please refer to the paragraphs headed “Audit Related and Other Issues – (E) Cash Transactions” and “Audit Related and Other Issues – (F) Purchase of Wood Logs” below for further details.

The Independent Board Committee further verified the bank balance of the Group by obtaining bank statements directly from all the commercial banks with which the Group maintains bank accounts.

The cash and bank balance of the Group as at 31 December 2010 was equivalent to approximately RMB2,777.0 million, of which (a) approximately RMB21.1 million and US\$166.1 million was maintained in the PRC; and (b) approximately HK\$5.7 million and US\$250.6 million was maintained in Hong Kong. Such cash and bank balance of the Group as at 31 December 2010 was disclosed in the announcement of the Company dated 29 April 2011 in relation to its results for the financial year ended 31 December 2010 (the “**Annual Results Announcement**”).

The cash and bank balance of the Group as at 25 February 2011 was equivalent to approximately RMB2,440.7 million, of which (a) approximately RMB152.1 million and US\$143.5 million was maintained in the PRC; and (b) approximately HK\$2.7 million and US\$204.1 million was maintained in Hong Kong. Such cash and bank balance of the Group as at 25 February 2011 was disclosed in the announcement of the Company dated 2 March 2011.

The cash and bank balance of the Group as at 22 April 2011 was equivalent to approximately RMB2,384.2 million, of which (a) approximately RMB190.5 million and US\$137.2 million was maintained in the PRC; and (b) approximately HK\$2.8 million and US\$200.2 million was maintained in Hong Kong.

*(iii) Measures taken by the Company*

As disclosed in the announcement of the Company dated 2 March 2011 (for items (a) to (d) below) and subsequent to such announcement (for item (e) and (f) below), the Company implemented the following internal control measures to strengthen its control over its bank accounts with commercial banks and the cash and bank balance maintained therein:

- (a) any cash payment, transfer of funds or other payments over RMB100,000 will require the written approval by the relevant authorized signatory and the approval by Mr. Li Kwok Cheong, the Chairman and an executive director;
- (b) any cash payment, transfer of funds or other payments over RMB1,000,000 will further require the approval by Mr. Xiao Feng, a non-executive director, and a notification to the Board;

- (c) any use of the bank balance of approximately US\$204 million (as of 25 February 2011) in the bank accounts of the Group maintained in Hong Kong is prohibited, except for conducting the day-to-day operations of the Group and payment of professional fees;
- (d) the cash and bank balance of the Group as set out in the relevant bank statements will be reviewed and analyzed on a weekly basis by an independent accounting firm;
- (e) authorized signatories of the bank accounts of the Group maintained in the PRC have been changed to Mr. Lin Pu, an executive director, or Mr. Li Kwok Cheong, the Chairman and an executive director, and where permissible, together with a member of the Independent Board Committee as a joint signatory, for any payment in excess of RMB1,000,000; and
- (f) authorized signatories of the bank accounts of the Group maintained in Hong Kong have been changed to Mr. Li Kwok Cheong, the Chairman and an executive director, together with a member of the audit committee or a member of the Independent Board Committee as a joint signatory, for any payment in excess of RMB1,000,000.

## **(B) Insurance Policies**

### ***(i) Issue***

In the course of the audit process of KPMG, the Former Management Team provided KPMG with copies of insurance policies maintained with a PRC insurer in respect of the forests of the Group. KPMG consulted the operations department of such PRC insurer and noted that there were inconsistencies between the information provided by the operations department of such PRC insurer to KPMG and the details set out in certain confirmation purportedly returned by such PRC insurer to KPMG.

### ***(ii) Relevant Findings by the Independent Board Committee***

In response to the queries made by the Independent Board Committee, Mr. Li Han Chun, the former chief executive officer and an executive director, represented that the Group did not purchase any insurance policies from such PRC insurer in respect of the forests of the Group for the year ended 31 December 2010, due to disagreement with such PRC insurer in relation to the amount of insurance premium payable.

In February 2011, the Company received from another PRC insurer an invoice for insurance premium in the amount of RMB6.0 million payable under an insurance policy in respect of certain forests of the Group for the year ended 31 December 2010. The Company paid the insurance premium in March 2011.

According to the above invoice and the particulars of the corresponding insurance policy provided by such PRC insurer, approximately 160,000 hectares of forests of the Group was under such insurance policy for the year ended 31 December 2010. There was no evidence that the rest of the forests of the Group was under any insurance policy for the year ended 31 December 2010. For the year ended 31 December 2010, the Board, having made all reasonable enquiries confirms that, to the best of its knowledge and belief, it is not aware of any material loss from damages on the forests of the Group.

**(iii) *Measures taken by the Company***

As at the date of this announcement, the Company is currently in negotiation with a PRC insurer to procure insurance policies to cover all forests of the Group for the year ending 31 December 2011.

**(C) Logging Permits**

**(i) *Issue***

In the course of the audit process of KPMG, the Former Management Team provided KPMG with copies of handwritten logging permits. KPMG noted that a substantial number of such handwritten permits appearing to be identical and manual chops appearing to be located in identical areas of each permit. KPMG consulted with the relevant PRC forestry bureau, which confirmed that the relevant logging permits should have been computer generated and not handwritten.

**(ii) *Relevant Findings by the Independent Board Committee***

As part of its investigation, the Independent Board Committee requested each relevant PRC forestry bureau regulating the logging activities of the Group to confirm if the relevant logging permits were issued by it and were genuine.

According to the confirmations obtained from the relevant forestry bureaus, for the year ended 31 December 2010:

- (a) logging permits in respect of approximately 100,000 m<sup>3</sup> of wood were falsified copies; and
- (b) all the remaining logging permits, the relevant PRC forestry bureaus were unable to make any comment, due to the fact that such PRC forestry bureaus did not have complete internal records in respect of the relevant logging permits.

Regarding the falsified logging permits in respect of the approximately 100,000 m<sup>3</sup> of wood, no logging activities were carried out in the relevant forests of the Group for the year ended 31 December 2010.

***(iii) Measures taken by the Company***

As at the date of this announcement, in respect of the logging activities of the Group for the year ending 31 December 2011,

- (a) the Group has obtained duly and validly issued logging permits in respect of 670,000 m<sup>3</sup> of wood from the relevant PRC forestry bureaus;
- (b) the Group is in the course of applying for logging permits in respect of an additional 300,000 m<sup>3</sup> of wood; and
- (c) the Board has resolved to establish a forest management team to monitor the logging activities of the Group to ensure compliance with the relevant logging permits and the relevant PRC laws and regulations.

**(D) Forest Ownership Certificates**

***(i) Issue***

In the course of the audit process of KPMG, the Former Management Team provided KPMG with copies of forest ownership certificates in respect of certain forests in Guizhou Province acquired by a Group Company in December 2010. KPMG noted that the issue dates shown on the relevant forest ownership certificates predated the establishment of the relevant Group Company.

***(ii) Relevant Findings by the Independent Board Committee***

As part of its investigation, the Independent Board Committee requested the Board to engage an independent PRC law firm (the “**PRC Legal Advisers**”) to ascertain the forest ownership rights owned by the Group.

The PRC Legal Advisers obtained direct confirmation from the Guizhou Forestry Bureau, which confirmed that (a) the issue dates shown on the relevant forest ownership certificates were the dates on which the forest ownership rights were granted by the Guizhou Forestry Bureau to the previous owners of the relevant forests; and (b) such issue dates were not updated due to administrative mistake when the relevant forest ownership rights were transferred to the Group.

*(iii) Measures taken by the Company*

In addition to the forest ownership certificates mentioned above, the Board instructed the PRC Legal Advisers to ascertain other forest ownership rights owned by the Group.

As part of the legal due diligence exercise, the PRC Legal Advisers, among other matters:

- (A) visited and interviewed with the officials of the forestry bureaus in the following locations:
  - (a) Meigu County of Sichuan Province,
  - (b) Mabian County of Sichuan Province;
  - (c) Ebian County of Sichuan Province;
  - (d) Jinkouhe District of Sichuan Province;
  - (e) Yingjing County of Sichuan Province;
  - (f) Liping County of Guizhou Province;
  - (g) Congjiang County of Yunnan Province;
  - (h) Changshun County of Guizhou Province;
  - (i) Wenshan Prefecture of Yunnan Province;
  - (j) Yanshan County of Yunnan Province;
  - (k) Ninglang County of Yunnan Province;
  - (l) Yunlong County of Yunnan Province;
  - (m) Yangbi County of Yunnan Province;
  - (n) Yingjiang County of Yunnan Province;
- (B) reviewed all relevant documents available in relation to the forest ownership rights in the Group's possession, including the original forest ownership certificates and contracts in respect of transfer of forest ownership rights; and
- (C) interviewed the relevant employees of the Group.

The Group has obtained confirmations with full particulars from each relevant forest bureau in respect of all forests of the Group. According to the above confirmations, as at 31 December 2010, the Group owned approximately 231,000 hectares of forests.

As at the date of this announcement, the details of the forest ownership rights of the Group are summarized below:

<b>Location</b>	<b>Area (Approximate)</b>
Yunnan Province	203,000 hectares
Sichuan Province	26,000 hectares
Guizhou Province	<u>2,000 hectares</u>
<b>Total:</b>	<b><u><u>231,000 hectares</u></u></b>

On the basis of the legal due diligence exercise, the PRC Legal Advisers are of the view that the Group has legally and validly acquired the above forest ownership rights and it has the rights to occupy, use and generate income from such forests within the period specified by the relevant forest ownership certificates.

## **(E) Cash Transactions**

### **(i) Issue**

As part of its investigation, the Independent Board Committee discovered that under the instructions of the Former Management Team led by Mr. Li Han Chun, the former chief executive officer and an executive director, almost all of the sales of the Group for the year ended 31 December 2010 were conducted by way of cash transactions.

### **(ii) Relevant Findings by the Independent Board Committee**

The Independent Board Committee is of the view that (a) the sales proceeds of these cash transactions might not have been deposited into the bank accounts of the Group and the sales revenue of these cash transactions might not have been entirely booked in the accounts of the Group previously presented to the Board; and (b) Mr. Li Han Chun, together with the former finance team under his control, maintained more than one set of books and accounts for these cash transactions and as a consequence, the actual cash movement was concealed from the Board.

The Independent Board Committee has been advised by certain employees of a Group Company, which generated a majority of the sales revenue for the Group for the year ended 31 December 2010, that Mr. Li Han Chun, together with the former finance team under his control, have removed certain books and records of such Group Company. Accordingly, the Independent Board Committee is of the view that it is likely impossible to ascertain the actual sales revenue of the Group for the year ended 31 December 2010.

**(iii) *Measures taken by the Company***

Since the Board became aware of the cash transaction practice of the Former Management Team in February 2011, the Board has immediately instructed the current management team that (a) such cash transaction practice should stop; (b) all future sales should be conducted by way of formal written contracts and settled by way of bank transfers or cheques; and (c) all future sales should be properly reflected in the management accounts of the Group.

The Board understands that the newly approached potential corporate customers of the Group have been informed of the new formal documented purchase procedures of the Group and they have preliminarily expressed that they are willing to follow such procedures.

The Board has reminded the employees of the Group that concealing the actual cash movement and bank balance of the Group from the Board by any means is a serious breach of employee's duties and obligations to the Group, which will lead to termination of employment.

Please refer to the paragraph headed "Audit Related and Other Issues – (A) Bank Statements and Bank-in Slips" above for further details of the newly implemented internal control measures to strengthen the Group's control over its bank accounts with commercial banks and the cash and bank balance maintained therein.

**(F) Purchase of Wood Logs**

**(i) *Issue***

In the course of its investigation, the Independent Board Committee discovered that the Group did conduct trading activities in respect of wood logs during the year ended 31 December 2010.

**(ii) *Relevant Findings by the Independent Board Committee***

The Independent Board Committee discovered that at the instructions of the Former Management Team, the Group purchased an aggregate of approximately 268,000 m<sup>3</sup> of wood logs at a cost of RMB534.8 million during the second half of 2010 by way of cash generated from cash transactions as described in the paragraph headed "Audit Related and Other Issues – (E) Cash Transactions" above.

In response to the queries made by the Independent Board Committee in respect of the purchase of wood logs, Mr. Li Han Chun, the former chief executive officer and an executive director, explained that by purchasing wood logs at appropriate prices instead of merely keeping cash generated from operations, the value of the Group's assets could be preserved against inflation risk and foreign exchange rate risk, in particular, in light of the foreseeable appreciation of the RMB against the US dollar.

In order to ascertain the existence and value of the wood logs purchased, the Independent Board Committee:

- (a) requested the Board to engage a professional valuer to conduct a physical stock-take at the locations where the wood logs were stored together with a team of management staff; such stock-take was attended by KPMG, an independent forensic accounting experts and an independent accounting firm;
- (b) requested the professional valuer to conduct a physical stock-take and assess the value of the wood logs; and
- (c) reviewed the documents in relation to the purchases (to the extent that they have not been removed by the Former Management Team and accessible by the Independent Board Committee), such as purchase contracts/orders, warehouse records and cash records.

***(iii) Measures taken by the Company***

The Board has procured insurance coverage, where permissible, in respect of the wood logs in order to protect the Group interest in such inventory. The Board believes that the Group possesses an established distribution channel for wood logs and there is a ready market for wood logs in China. Taking into account of the general economic environment and the trend of market prices of wood logs in China, the Board considers that the rationale behind the purchase of wood logs as explained by Mr. Li Han Chun may be commercially sound. Therefore, the Board is evaluating the prospect of, and may continue to conduct, trading activities in respect of wood logs.

## UPDATE ON THE MEMBERS OF THE SENIOR MANAGEMENT TEAM

### (i) Former Management Team

The Independent Board Committee is of the view that the Former Management Team was the source of the above irregularities reported by it or KPMG.

Upon the recommendations of the Independent Board Committee, the Board has resolved that:

- (a) Mr. Li Han Chun be dismissed from his position of the chief executive officer of the Group with effect from 14 February 2011;
- (b) Ms. Wu Xiaofen be dismissed from her position of the joint chief financial officer of the Group with effect from 31 March 2011;
- (c) Mr. Zhang Hongyu be dismissed from his position of the chief resource officer of the Group with effect from 31 March 2011;
- (d) Ms. Lv Aoqian be dismissed from her position of the chief human resource officer of the Group with effect from 31 March 2011;
- (e) the resignation tendered by Mr. Wen Guoping from his position of the joint chief financial officer of the Group with effect from 15 March 2011 be approved; and
- (f) the resignation tendered by Mr. Li Haijun from his position of the chief sales officer of the Group with effect from March 2011 be approved.

The Company confirms that none of the above members of the Former Management Team has had any executive and/or administrative roles in the Group since the above effective dates and none of them has reported to work since mid-February 2011. Mr. Li Han Chun remains as an executive director of the Company, the removal of whom or not is within the power of the shareholders of the Company in general meeting.

The Company is seeking legal advice as to whether any legal actions should be taken against any or all of above members of the Former Management Team in respect of the matters disclosed herein.

## (ii) Current Management Team

The current management team of the Group comprises of the following members:

- (a) Mr. Li Jian was appointed as the acting chief executive officer of the Group in place of Mr. Li Han Chun and is responsible for overseeing the entire business operations of the Group;
- (b) Mr. Lin Pu, an executive Director, was appointed as a vice president of the Company and is responsible for potential acquisition of forests and local business operations of the Group in Yunnan Province, Guizhou Province and Sichuan Province;
- (c) Mr. Michael Cheung was appointed as a vice president of the Group and is responsible for financial management, investor relationships and financial reporting of the Group and assisting the acting chief executive officer in formulating the Group's strategy;
- (d) Mr. Wei Bin was appointed as the general manager of a PRC subsidiary of the Group in Sichuan Province and is responsible for overseeing the entire business operations of the Group in the Sichuan Province.

Mr. Wei has over 15 years of experience in investment management and financial services. Prior to joining the Group, he was the general manager of Hebei Fulin Investment Management Company (河北富林投資管理公司), a company principally engaged in investment management in the PRC from 2007 to 2011. From 2003 to 2007, he was a manager of the investment department of Bohai Trust Company Limited (渤海信托有限公司).

- (e) Mr. Xu Jiazeng was appointed as the financial controller of the Group for its business operations in the PRC and is responsible for financial management and financial reporting of the PRC subsidiaries of the Group.

Mr. Xu is a member of the Chinese Institute of Certified Public Accountants and the American Institute of Certified Public Accountants. He is also a Certified Internal Auditor. He has over 10 years of experience in accounting and financial consulting. Prior to joining the Group, Mr. Xu was a senior manager at Resources Global Professionals and was responsible for financial due diligence and consulting from 2009 to 2011. From 2007 to 2009, he was a manager of Deloitte Consulting (Shanghai) Co., Ltd., Beijing Branch. From 1999 to 2007, he was employed at the audit department and corporate consulting departments of Ernst & Young, an international accounting firm.

The Company is in the process of recruiting suitable replacements for other vacancies arising from the above dismissals and resignations.

By Order of the Board  
**China Forestry Holdings Co., Ltd.**  
**Li Kwok Cheong**  
*Chairman*

Hong Kong, 29 April 2011

*As at the date of this announcement, the executive directors of the Company are Mr. Li Kwok Cheong, Mr. Li Han Chun and Mr. Lin Pu, the non-executive directors of the Company are Mr. Xiao Feng, Mr. Li Zhi Tong and Mr. Meng Fanzhi, and the independent non-executive directors of the Company are Mr. Wong Tak-jun, Mr. Liu Can and Mr. Zhu Demiao.*