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枫叶教育

CHINA MAPLE LEAF EDUCATIONAL SYSTEMS LIMITED

中國楓葉教育集團有限公司*

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 1317)

INSIDE INFORMATION KEY FINDINGS OF INDEPENDENT INVESTIGATION

This announcement is made by China Maple Leaf Educational Systems Limited (the “**Company**”, together with its subsidiaries and consolidated affiliated entities, the “**Group**”) pursuant to Rule 13.09(2) of the Listing Rules and the Inside Information Provisions (as defined in the Listing Rules) under Part XIVA of the Securities and Futures Ordinance.

References are made to the announcements of the Company dated 27 April 2022, 16 May 2022, 23 May 2022, 30 May 2022, 14 June 2022, 18 July 2022, 25 July 2022, 2 August 2022, 1 November 2022, 30 November 2022, 1 February 2023, 14 April 2023, 18 April 2023, 28 April 2023, 19 June 2023 and 28 June 2023 (collectively, the “**Announcements**”) in relation to, among other matters, (i) the delay in publication of the 2022 Interim Results; (ii) the Suspension; (iii) the establishment of the IBC and the appointment of the Independent Investigator; (iv) the Resumption Guidance; (v) the resignation of auditor of the Company; (vi) the appointment of auditor of the Company; (vii) the quarterly update on resumption progress; (viii) the delay in publication of the 2022 Annual Results; (ix) the update in relation to compliance with certain conditions of the Bonds; (x) the relevant event in relation to the Bonds; and (xi) the delay in publication of the 2023 Interim Results. Unless otherwise defined, capitalised terms used in this announcement shall have the same meanings as those defined in the Announcements.

BACKGROUND

Trading in the shares of the Company on the Stock Exchange and the debt securities of the Company has been suspended with effect from 9:00 a.m. on 3 May 2022 due to the delay in publication of the 2022 Interim Results.

On 13 May 2022, the Company received the Letter from Shinewing (HK) CPA Limited (“**Shinewing**”), the former auditor of the Company, regarding the Relevant Matters identified during the course of its review of the 2022 Interim Results.

In order to address and resolve the Relevant Matters as soon as practicable, on 22 May 2022, the Board resolved to establish the IBC which shall exercise powers, authorities and discretions as delegated by the Board for:

- (i) conducting an independent investigation into the Relevant Matters (the “**Independent Investigation**”) and engaging an independent third-party investigator to assist it with the Independent Investigation;
- (ii) exploring the Group’s adoption of, or improvements on, internal control system, procedures and mechanisms, where necessary;
- (iii) engaging and/or generally obtaining advice from legal and/or financial professionals and/or experts in connection with the above purposes; and
- (iv) making recommendations to the Board on appropriate actions to be taken.

On 27 May 2022, the Stock Exchange has set out various Resumption Guidance for the Company, among which, the Company shall conduct an independent forensic investigation into the Relevant Matters set out in the Letter (i.e. the Independent Investigation), announce the findings and take appropriate remedial actions.

With the recommendation of the IBC, the Board, on 13 June 2022, appointed the Independent Investigator, an independent forensic accountant, to conduct the Independent Investigation covering the Relevant Matters and prepare an investigation report on the findings of the Independent Investigation and provide recommendations to the IBC in respect of the Relevant Matters (the “**Investigation Report**”).

The Company wishes to update the Shareholders that the Independent Investigator has completed the Independent Investigation and issued the Investigation Report to the IBC on 20 June 2023. The IBC, comprising all independent non-executive Directors, namely Mr. King Pak Lau, Mr. Peter Humphrey Owen, Mr. Alan Shaver and Ms. Wai Fong Wong, having reviewed the findings and results of the Independent Investigation, presented the Investigation Report, together with the recommendations of the IBC, to the Board for consideration and approval on 20 June 2023.

SCOPE OF THE INDEPENDENT INVESTIGATION

In addressing the Resumption Guidance from the Stock Exchange, the Independent Investigator conducted the Independent Investigation covering the matters surrounding the Relevant Matters.

Key review approach performed by the Independent Investigator in the Independent Investigation include, but not limited to, the following:

- (i) obtaining explanations, information and documents of the Company in relation to the Relevant Matters;
- (ii) performing analytical review on the obtained explanations, information and documents;

- (iii) performing company searches and/or internet searches on the parties involved in the Relevant Matters;
- (iv) conducting site visits to selected schools and school canteens;
- (v) interviewing key individuals including but not limited to selected Canteen Subcontractors, directors and staff of the Company; and
- (vi) obtaining and reviewing electronic data from various custodians' computer, email box and network folder subject to their relevance and availability (the “**Computer Forensic Review**”).

MAJOR LIMITATIONS OF THE INDEPENDENT INVESTIGATION

The findings of the Independent Investigation are subject to certain limitations. The key limitations include but not limited to:

- (i) According to the Company, Mr. Li Wanqing (李萬慶) (“**Mr. WQ Li**”) was the former vice chairman of the Group and the legal representative and executive director of Dalian Maple Leaf Catering Service Company Limited* (大連楓葉餐飲服務有限公司) (the “**Catering Company**”) and he was the most knowledgeable person within the Group in respect of the management fee received during the Period given that Mr. WQ Li was the sole and ultimate decision maker of the Catering Company or the catering business of the Group at the material time, and all major and important business decisions in respect of the catering business of the Group were made by him at the material time. Regrettably, Mr. WQ Li passed away in May 2022 before the commencement of the Independent Investigation, and hence, the Independent Investigator could not obtain any direct information, document and/or explanation from Mr. WQ Li.
- (ii) Regarding the Computer Forensic Review, the Independent Investigator was informed by the Company that the computers of Mr. Shu Liang Sherman Jen (任書良) (an executive Director, the chairman of the Board, the chief executive officer of the Company and the president of China Operations) (“**Mr. Sherman Jen**”), Ms. Jingxia Zhang (張景霞) (an executive Director and the chief financial officer of the Company) (“**Ms. JX Zhang**”), Ms. Ying Gao (高瑩) (the financial controller of the Group), Ms. Shuling Jen (任書玲) (the assistant to the chief financial officer of the Company, the company secretary of the Company and the director of Tech Global Investment Limited (特高投資有限公司) (“**Tech Global**”)) (“**Ms. Grace Jen**”) and Mr. Yanbo Wang (王衍波) (the legal representative, executive director and manager of the Catering Company) (“**Mr. YB Wang**”) were personal computers which the Company could not make available for its inspection. Notwithstanding the aforesaid, Mr. Sherman Jen and Ms. JX Zhang voluntarily provided with the Independent Investigator their personal laptop computers for computer forensic review, whereas Ms. Ying Gao, Ms. Grace Jen and Mr. YB Wang declined to hand out their computer for computer forensic review due to privacy concerns. Nevertheless, the Company has retrieved from its email server the emails sent or received by Ms. Ying Gao, Ms. Grace Jen and Mr. YB Wang through their company email accounts with domain “mapleleaf.net.cn” and provided with the Independent Investigator the said emails for computer forensic review.

SUMMARY OF KEY FINDINGS

Matter 1 – Management fee received from the Canteen Subcontractors amounted to RMB32 million for the Period

- (i) The Catering Company entered into cooperation agreements (餐飲公司、食堂合作協議書) (the “**Cooperation Agreements**”) and supplemental cooperation agreements (餐飲公司、食堂合作補充協議) (the “**Supplemental Cooperation Agreements**”) with various Canteen Subcontractors in relation to the canteen management services provided by the Catering Company to the Canteen Subcontractors. The Catering Company received management fees from the Canteen Subcontractors accordingly (the “**Management Fees**”).
- (ii) **Significant growth in the Management Fees**
- (I) The Management Fees for the six months ended 28 February 2021 and 31 August 2021 amounted to approximately RMB4.7 million and RMB4.5 million respectively, (i.e. equivalent to 5% of the school canteens’ turnover); whereas the Management Fees for the Period amounted to approximately RMB32 million (i.e. equivalent to 45% of the school canteens’ turnover).
- (II) The late Mr. WQ Li was entrusted and/or delegated to manage and acted as the ultimate controller and/or decision maker of the Catering Company. Mr. WQ Li held absolute power and control over the Catering Company from its incorporation on 26 May 2015 until his passing in May 2022.
- (III) Low Management Fees in the financial year ended 31 August 2020 (“FY19/20”) and the financial year ended 31 August 2021 (“FY20/21”)
- (a) The Management Fees consisted of two parts, namely basic management fees and additional management fees. While the basic management fees remained unchanged at 5% all the time, the additional management fees varied depending on the services provided every year. Mr. WQ Li decided only to charge the basic management fees of 5% without charging any additional management fees for FY19/20 and FY20/21 because of the Covid-19 pandemic.
- (b) Both the basic management fee rate or the additional management fee rate were not specified in the Cooperation Agreement. The total management fees rate of 45% was specified in the Supplemental Cooperation Agreements.

(IV) Extended and enhanced services pursuant to the Supplemental Cooperation Agreements

- (a) According to the Cooperation Agreements, the Catering Company would provide seven canteen management services to the Canteen Subcontractors. Pursuant to the Supplemental Cooperation Agreement, four new services would be added and two existing services would be enhanced for the period from 1 September 2021 to 31 August 2022. In consideration of the extensions and enhancements of the services, the Management Fees would be increased to 45% of the revenue of the school canteens.
- (b) However, due to the Covid-19 pandemic, the Catering Company was unable to provide some of the new services as planned or agreed.

(V) Smart canteen system

- (a) Mr. WQ Li had intended to install smart canteen system for the school canteens in the financial year ended 31 August 2022 (“FY21/22”) to guarantee the food safety and lower the costs of the canteens.
- (b) The smart canteen system would cost around RMB25 million to RMB30 million in 2021. In order to finance the installation costs of the smart canteen system, Mr. WQ Li decided to implement a one-off increase in Management Fees to 45% for FY21/22.

(VI) Reduction of the Management Fees

- (a) Given that the smart canteen system ended up not being implemented due to the passing of Mr. WQ Li in May 2022, in around August 2022, Ms. JX Zhang decided to reduce the Management Fees for FY21/22 and FY22/23 from 45% to 15%.
- (b) The excess payments made by the Canteen Subcontractors amounting to approximately RMB13.2 million as at 31 August 2022 were not refunded to the Canteen Subcontractors but treated as Management Fees received in advance instead.
- (c) Due to the retrospective reduction of the Management Fees from 45% to 15%, the excess amount paid by the Canteen Subcontractors will be applied to offset with the Management Fees in future and the Canteen Subcontractors did not make any objection to that.

(iii) **The Cooperation Agreements and the Supplemental Cooperation Agreements were undated and had no identification information other than the name**

(I) The Company explained that the identification information of the Canteen Subcontractors was not a “must-have” element of an agreement and provided that, given the subcontractors were individuals, the Cooperation Agreements should be legally valid if they were signed by the Canteen Subcontractors, as opined by Guangdong Guanghe Law Firm* (廣東廣和律師事務所) (“**GD Guanghe**”).

(II) Signing arrangement

(a) Most of the Cooperation Agreements and the Supplemental Cooperation Agreements were signed by various staff members of the Group on behalf of the Canteen Subcontractors using the respective Canteen Subcontractors’ names (rather than their own) (the “**Signing Arrangements**”).

(b) The Canteen Subcontractors had issued various authorisation letters (the “**Authorisation Letters**”) to authorise the respective staff members of the Group to execute the Cooperation Agreements and any supplemental cooperation agreements on their behalf.

(c) The Authorisation Letters were in fact issued by the Canteen Subcontractors after the execution of the Cooperation Agreements and were backdated to various dates before the execution date shown on the Cooperation Agreements (i.e. the Authorisation Letters had not existed or were not signed by the Canteen Subcontractors when the Cooperation Agreements were executed by the staff of the Group on behalf of the Canteen Subcontractors).

(d) The Canteen Subcontractors who attended interviews were of the view that the credibility of Mr. WQ Li as well as the Group was even more important than the agreements. Also, given that operating school canteens is considerably profitable, many others are keen to cooperate with the Group and the Group could easily find replacement of the Canteen Subcontractors. Hence, they considered themselves not having much bargaining power on the requests made by the Catering Company and/or the Group; perhaps the respective schools. They would like to maintain long term cooperation with the Group and would submit themselves to Group’s requests in order to avoid offending the Group. Therefore, they agreed to sign the arrangements and subsequently issued and/or signed the respective backdated Authorisation Letter at the Catering Company’s request.

(iv) **Management Fees were settled by the Affected Schools**

(I) The school canteens are nominally operated by the schools, and according to the food operation permits (食品經營許可證), operator of the school canteens were the schools while the legal representatives (responsible persons) were the headmasters of the schools or the senior management of the Group, such as Mr. Sherman Jen and Ms. JX Zhang.

- (II) The Canteens Subcontractors were unable to open bank accounts under the name of the school canteens and the said bank accounts (the “**Canteen Bank Account**”) could only be opened by the canteen operators (i.e. the schools). On the other hand, it is prohibited by the PRC law for the Canteen Subcontractors to carry out business transactions through personal bank accounts. Therefore, the Canteen Subcontractors had to use the Canteen Bank Accounts for the receipts and payments of funds in relation to the canteens’ operations.
- (III) Based on the legal advice obtained by Dalian Maple Leaf Educational Group Company Limited* (大連楓葉教育集團有限公司) (“**Dalian ML Group**”) from Beijing Jingtian Gongcheng (Chengdu) Law Firm* (北京市競天公誠(成都)律師事務所) (“**JTGC**”), neither the schools nor the Canteen Subcontractors would be able to operate the Canteen Bank Accounts without the other side’s consent.
- (IV) Both the Company and the Canteen Subcontractors stated that the funds in the Canteen Bank Accounts belonged to the Canteen Subcontractors instead of the schools or the Group. This is echoed by the legal advice of JTGC.
- (v) **The Canteen Subcontractors were addressed as “Canteen Managers”**
- (I) Since the canteens were run by the Canteen Subcontractors who are natural person individuals, it was the usual practice to address the subcontractors as “經理” (literally “**manager**”) following their surname. It would quite awkward to address them as “承包商” (literally “**subcontractor**”) in daily communications.
- (vi) **No increment in corresponding cost**
- (I) The Company explained that the primary reason of the increase in the Management Fees to 45% was to cover the costs of the contemplated installation of the smart canteen system. Since the smart canteen system had not been purchased yet, such costs had not been incurred by the Catering Company for the six months ended 28 February 2022.
- (II) In addition, only limited extended and/or enhanced services were performed by the Catering Company and the Company stated that most of them were performed by the existing staff of the Catering Company, therefore, no significant costs were incurred for that.
- (vii) **Two sets of accounting voucher**
- (I) The treasurer of the Catering Company, Ms. Ling Yu (于玲) (the treasurer of the Catering Company), stated that the said two sets of accounting vouchers were prepared by her. The initial set of vouchers was the one with the description “Recognition of 2019-2021 school year accrued management fee”. She stated that it was prepared according to the instructions of Mr. WQ Li and the calculation was based on the turnover of certain school canteens in FY19/20 and FY20/21.

- (II) Mr. Ling Yu further stated that Mr. WQ Li subsequently clarified with her that the correct nature of the transaction was the recognition of the additional management fees for the period from 1 September 2021 to 28 February 2022 pursuant to the Supplemental Cooperation Agreements.

(viii) **Conclusion**

- (I) According to the Supplemental Cooperation Agreements, the Catering Company's provision of new or enhanced services to the Canteen Subcontractors led to the significant increase of the Management Fees from 5% to 45% during the Period. However, due to lack of documentation, there was insufficient evidence to support the company's initial intentions and planned timeline for offering these services.
- (II) Also, the arrangement of the signing/execution of the Supplemental Cooperation Agreements was crude or primitive and/or lack of proper arrangement including but not limited to backdating and/or signing via informalised power of attorney.
- (III) The entire process from drafting to signing of the Supplemental Cooperation Agreements to the subsequent performance of the Supplemental Cooperation Agreements had been lack of documentation and records including the asserted core reason of the increase in management fee or revenue sharing.
- (IV) However, interviews with the Canteen Subcontractors revealed that their trust and confidence in Mr. WQ Li, coupled with their evaluation of profitability associated with the ongoing operating of the canteen at each school, played pivotal roles in their decision to accept or enter into the Supplemental Cooperation Agreement.
- (V) Moreover, it would also appear that the Canteen Subcontractors acknowledged their limited bargaining power with the school (and/or the school and Catering Company acting together) because they could not operate without the school's consent and commercially, they had been making decent profit (including taking into account that they had paid 10 to 20 plus percent of revenue sharing in the past).
- (VI) This seems to be the possible reasons which caused the deviation between the agreement and the actual performance, the lack of documentation in support of the negotiation, the primitive arrangement and the drastic increase of the management fees. Lastly, no evidence has been identified at this stage suggesting that the Company had suffered any financial loss as a result of this incident.
- (VII) Further, given that the smart canteen system ended up not being implemented due to the passing of Mr. WQ Li in May 2022, in around August 2022, Ms. JX Zhang decided to reduce the Management Fees for FY21/22 and FY22/23 from 45% to 15%. The excess payments made by the Canteen Subcontractors were treated as Management Fees received in advance and will be applied to offset with the Management Fees in future.

Matter 2 – Royalty income from the Affected Schools for the CIP Use Rights amounted to RMB23 Million for the Period

(i) **New royalty income**

- (I) In around February 2021, the Group intended to transfer some of the characteristic intellectual properties (the “**CIP**”) owned by the Group to Tech Global. Tech Global would then charge the schools within the Group royalty fees for the use of the CIP, and when conditions were ripe, the CIP could be exported to schools outside the Group.
- (II) Ms. Ying Gao stated that she commenced the preparation work and preliminarily discussed with Mr. Jian Zhang (張健) in March 2021 about the content of the CIP contracts. However, only until mid-August 2021, Ms. Ying Gao calculated the royalty fee to be paid by each relevant school and requested the finance staff of each relevant school through Tencent QQ to confirm the respective total income of tuition fee income and accommodation fee for the year ended 31 December 2020.
- (III) In late August 2021, Ms. Ying Gao and Mr. Jian Zhang (the assistant to the chief financial officer of the Company and the financial controller of a subsidiary of the Company) finalised the CIP Use Rights contracts (the “**CIP Contracts**”) to be entered into between Tech Global and 25 schools (the “**CIP Schools**”), 23 of which were the Affected Schools (the “**Affected CIP Schools**”). Meanwhile, Ms. Ying Gao verbally informed the finance staff of each CIP Schools via telephone that she had reversed the closed accounts (反結賬) of Yonyou System (用友系統) of March 2021 and recorded the royalty fees for the use of the CIP as “Costs of sales” for each of the CIP Schools by the journal entries dated 31 March 2021. The said accounting entries were backdated to 31 March 2021.
- (IV) On 8 September 2021, Ms. Ying Gao affixed the electronic chop of Tech Global to the CIP Contracts and sent the CIP Contracts together with the invoices for the royalty fees to the CIP Schools, except Huaian Enlai Maple Leaf Bilingual School* (淮安恩來楓葉雙語學校) (“**Enlai Bilingual**”), by email.
- (V) The CIP Contracts were dated 1 March 2021 and the accounting entries were dated 31 March 2021 since it was agreed at the meeting in February 2021 that the royalty fees would be charged by Tech Global to the CIP Schools in March 2021, notwithstanding that the CIP Contracts were entered into in September 2021.
- (VI) On 9 September 2021, Dalian ML Group filed the application to the Liaoning Province Copyright Office (the “**Copyright Office**”) and on around 17 September 2021, the CIP were registered under Dalian ML Group.

- (VII) Ms. Ying Gao stated that she, having considered that the registration of the CIP under Tech Global had not been completed in FY20/21, on 13 September 2021, instructed the Group's finance staff, namely Ms. Chen Chen (陳晨), to record accounting entries dated 31 August 2021 through the accounting system used by the Group for consolidation, namely SunSystems, to reverse the royalty fees at the consolidated level, and by then, SunSystems automatically re-booked the royalty fees as the expenses in FY21/22.
- (VIII) On 24 September 2021, Dalian ML Group entered into a CIP transfer agreement with Tech Global and transferred the CIP to Tech Global for no consideration.
- (IX) On 27 September 2021, Dalian ML Group made applications to the Copyright Protection Centre of China* (中國版權保護中心) (the "CP Centre") for transfer of the ownerships of all the 13 CIP to Tech Global. The transfers of the 13 CIP were registered on 4 November 2021.
- (X) In other words, when entering into the CIP Contracts, Tech Global did not have the ownerships of the CIP and even the CIP had not been registered with the Copyright Office.

(ii) **Basis of determination of the Royalty Income**

- (I) The basis of the royalty income was made to a transfer pricing report prepared by Deloitte (the "TP Report") when determining the rate of the royalty income. Based on the TP Report, the first quartile, median and third quartile of the CIP Use Rights fee were 5.75%, 8% and 9.5% of the gross revenue respectively.
- (II) Tech Global charged the royalty fee at 2% or 3% of the gross revenue (i.e. tuition fee and accommodation fee) of the schools, which was lower than the first quartile rate in the TP Report. The royalty fees were calculated based on the gross revenue of the CIP Schools for the previous year, i.e. the year ended 31 December 2020.

(iii) **No duration of the CIP Use Rights**

- (I) According to the TP Report, the royalty fees should be based on the revenue of the schools, while the right of use of the CIP appeared to be perpetual and the schools could continuously generate income by using the CIP, it does not sound commercially reasonable for Tech Global to charge the royalty fees based on the tuition fees and accommodation fees revenue of the CIP Schools for only one year (i.e. 2020) for the perpetual right of use in the sense that the royalty fees would be disproportional with the revenue from the CIP. Ms. Ying Gao stated that it was her interpretation that the royalty fee was a one-off fee.

(iv) **Adjustment of the accounting treatment**

- (I) Ms. JX Zhang realised that the royalty income was billed and settled after the Regulations on the Implementation of the Non-state Education Promotion Law of the People’s Republic of China (2021 Revision)* (中華人民共和國民辦教育促進法實施條例(2021修訂)) (the “**Implementation Regulations**”) became effective on 1 September 2021.
- (II) Pursuant to section 45 of the Implemental Regulations, the Affected Schools were prohibited to conduct transactions with their related parties. Ms. JX Zhang was of the view that Tech Global should not carry out the royalty income related transactions and instructed Ms. Ying Gao in late April 2022 to adjust the gross amount paid by the Affected CIP Schools for the use of the CIP (i.e. royalty fees of RMB23 million plus the withholding taxes of RMB4 million) to “Other Payable to the Affected CIP Schools” at the consolidation level.
- (III) Tech Global recorded the relevant tax payments of approximately RMB4 million as tax expenses, however, it was of the view that the corporate income tax, value added tax and additions should be refunded to Tech Global having considered that Tech Global ultimately did not charge and receive the CIP Schools any royalty fee.

(v) **Conclusion**

- (I) The royalty income encapsulates the earning charged by Tech Global to the CIP Schools, which include the 23 Affected Schools along with two non-Affected Schools for the utilisation of the CIP.
- (II) Ms. Ying Gao stated that the duration of use rights was omitted in the CIP Contract because in her capacity as the drafter of the CIP Contracts. She deemed it unnecessary to stipulate a duration, with her belief based on the understanding that the CIP Schools had been granted unlimited access to the CIP.
- (III) Subsequently, the royalty income was reclassified as “Other Payable to Affected Schools”. This change was made when Ms. JX Zhang discovered that the royalty income was billed by Tech Global and settled by the CIP Schools after the enforcement of the Implementation Regulations on 1 September 2021 and expressed her concern about the potential non-compliance with the Implementation Regulations relating to the receipt of royalty income during the Period.
- (IV) Ms. Ying Gao in collaboration with Mr. Jian Zhang drafted the CIP Contracts in August 2021 and arranged for the CIP Schools to endorse the CIP Contracts in September 2021. To cover up her delay in the collection of royalty income, an action mandated by Ms. JX Zhang in February 2021, Ms. Ying Gao antedated the CIP Contracts to 1 March 2021. Further, she backdated the accounting entries that recorded the accrued royalty fees payable by the CIP Schools to March 2021, thus creating the impression that the royalty income transactions occurred in March 2021.

- (V) Considering that the CIP was neither registered with the Copyright Office nor transferred to Tech Global by March 2021, there exist doubts about the legitimacy and appropriateness of backdating the CIP Contracts and the related accounting entries.
- (VI) Notwithstanding the aforesaid, the transactions have been reversed and rectified. Tax expenses of RMB4 million arising from the royalty income were incurred by Tech Global, which in essence the financial loss suffered by the Group at this stage. In the event that the tax payments are fully refunded to Tech Global, the tax expenses will be completely reversed and the Group will no longer suffer any loss.

Matter 3 – Acquisition of the investment property at a consideration of RMB40 million during the Period

(i) Fund flows and accounting entries

- (I) In May 2018, Mr. Sherman Jen decided to purchase two properties from Dongguan Yitian Aocheng Real Estate Investment Co., Ltd.* (東莞市益田奧城房地產投資有限公司) (“**Yitian Aocheng**”). Meanwhile, the Company had offshore liquidity needs in around May 2018 for its overseas acquisition plan.
- (II) In light of the above, Mr. Sherman Jen paid a sum of HK\$71,074,076.34 (equivalent to RMB58 million) to the Company on 29 May 2018 to meet the Company’s offshore liquidity needs. On the other hand, the Company arranged Dalian Maple Leaf International School* (大連楓葉國際學校) (“**Dalian High School**”) to settle the balance of purchase price of the properties in a sum of RMB58 million (advance payment of RMB2 million was paid by Mr. Sherman Jen) to Yitian Aocheng on behalf of Mr. Sherman Jen on 29 May 2018 (the “**Funding Arrangement**”).
- (III) Subsequently, Mr. Sherman Jen stated that he had intended to transfer or sell one of the properties (the “**Property**”) to the Group to support the Group’s long-term development. Mr. Sherman Jen transferred the ownership of the Property to an indirect subsidiary of the Company, namely Dalian Maple Leaf Science and Education Company Limited* (大連楓葉科教有限公司) (“**Dalian S&E**”) through Yitian Aocheng’s internal ownership transfer procedure.
- (IV) Mr. Sherman Jen would like to receive Hong Kong dollar for the settlement of the consideration, and as such, HK\$48,728,194 (equivalent to RMB40 million) was paid to Mr. Sherman Jen by the Company on behalf of Dalian S&E on 10 November 2021.
- (V) In light of the above, there was no payment made to the property developer during the Period and there was no prepayment for fixed assets or amount due to director recorded in the previous years’ financial statements.

- (VI) On 30 August 2022, the Company offset the amount due from the Company to Dalian High School with the amount due from Dalian S&E to the Company. On 31 August 2022, Dalian S&E (subsequently known as Dalian Youwen Educational Technology Company Limited* (大連優文教育科技有限公司) (“**Dalian Youwen**”) recorded the intergroup transactions accordingly.
- (VII) On 29 August 2022, Dalian S&E paid RMB40 million to Dalian High School for the settlement of the amount due to Dalian High School.
- (VIII) Based on the accounting ledgers of the Company, there was an amount due to Dalian High School of HK\$22,345,882.34 as at 29 August 2022. On the other hand, based on the accounting ledgers of Dalian High School, there was an amount due from the Company of RMB18 million as at 29 August 2022.
- (IX) The Company settled an amount due from the Company to Dalian High School by a company in the PRC entrusted by Mr. Sherman Jen. On 30 August 2022, the Company paid HK\$22,345,882.34 to Mr. Sherman Jen and on 31 August 2022, Shenzhen Yuansi Education Service Company Limited* (深圳源思教育服務有限公司) paid an amount of RMB18 million to Dalian High School.
- (X) Notwithstanding the above, it is noted that the exchange rate on 30 August 2022 was approximately 1.1359 and based on such exchange rate, RMB18 million was equivalent to approximate HK\$20,445,300 on 30 August 2022. Therefore, the Company had paid an excess amount of approximately HK\$1,900,582.34 to Mr. Sherman Jen for the settlement of RMB18 million.
- (XI) On 12 June 2023, Mr. Sherman Jen refunded the excess amount he received of HK\$1,900,582.34 to the Group.

(ii) **Disclosure of the related party transactions**

- (I) The Company admitted that the transfer of the Property from Mr. Sherman Jen to Dalian S&E was a related party transaction whose nature and amount should have been disclosed in the Company’s financial statements pursuant to Hong Kong Accounting Standard 24 – Related Party Disclosures.
- (II) Pursuant to Chapter 14A of the Listing Rules, as Mr. Sherman Jen, being the Company’s Chairman and Executive Director, is a connected person of the Company. The purchase of the Property from Mr. Sherman Jen shall constitute a connected transaction and is subject to disclosure requirement.

(iii) **Approval policies and procedures**

- (I) There was no board resolution approving such significant acquisition of the Property or adequate approval on OA system for contract signing and payment process.

(iv) **Market value of the Property**

- (I) Property valuation was not performed before Dalian S&E purchased the Property. During the Independent Investigation, Dalian S&E engaged Kroll to assess the market value of the Property as at 1 November 2021 (the “**Kroll Report**”). Based on the Kroll Report, the market value of the Property as at 1 November 2021 was RMB40,900,000, which was RMB900,000 or 2.25% higher than the purchase price of Dalian S&E.

(v) **Conclusion**

- (I) There was no payment made to the property developer during the Period because the Property was in fact transferred to Dalian S&E by Mr. Sherman Jen instead of the property developer.
- (II) Mr. Sherman Jen paid HK\$71 million (equivalent to RMB58 million) to the Company in Hong Kong and Dalian High School paid RMB58 million on behalf of Mr. Sherman Jen to the property developer for his purchase cost of properties in May 2018. No prepayments for fixed assets or amount due to director were recorded in the book or disclosed in the previous years’ financial statements because the said fund transfers were neither prepayments for the Group’s purchase of property nor loans from Mr. Sherman Jen. Instead, it was a Funding Arrangement between the Company and Dalian High School with the assistance of Mr. Sherman Jen.
- (III) In November 2021, Dalian S&E purchased the Property from Mr. Sherman Jen at a consideration of RMB40 million. Such consideration was settled by the Company on behalf of Dalian S&E to Mr. Sherman Jen in Hong Kong. However, no board resolution of the Company was passed to approve the purchase of the Property. In addition, the Company had failed to publish an announcement pursuant to the Listing Rules for the purchase of the Property from Mr. Sherman Jen as a connected transaction.
- (IV) Based on the Kroll Report, there is no evidence which suggests that the Group has suffered any financial loss in the purchase of the Property.
- (V) Similarly, in August 2022, the Company paid an amount of HK\$22,345,882.34 for the settlement of the amount due to Dalian High School of RMB18 million by a similar funding arrangement through Mr. Sherman Jen. Given Mr. Sherman Jen only provided a channel to facilitate the fund transfer from the Company to Dalian S&E and the amount paid to and received from Mr. Sherman Jen offset each other, the Company did not regard the said transfers from and to Mr. Sherman Jen as amount due to or from Mr. Sherman Jen, rather, they were recorded as intercompany transfers from the Company to Dalian High School. As discussed above, an excess amount of HK\$1,900,582.34 had been paid to Mr. Sherman Jen in such arrangement and that the said excess amount of HK\$1,900,582.34 was refunded in full by Mr. Sherman Jen to the Company on 12 June 2023.

Matter 4 – Amount due from/to the Affected Schools

(i) Changes in the balance with related parties

- (I) The breakdown shows that four categories, namely borrowings, capital expenditure, interest accruals on borrowings and reversal of the royalty income, accounted for RMB241 million of the increase in amount due to related parties during the Period.
- (II) The Company obtained a legal opinion from GD Guanghe dated 24 May 2022 on whether lending of idle money from the Affected Schools to others would constitute any non-compliance with the Implementation Regulations. GD Guanghe advised that it was not specified by the law whether money lending was a related party transaction and based on “Whatever is not prohibited by law is permitted” principal, lending of idle money from the Affected Schools to others should not be regarded as related party transaction.
- (III) Notwithstanding the aforesaid, GD Guanghe further advised that, to be on the safe side, the Affected Schools should avoid lending money to related parties. GD Guanghe also advised that if the Affected Schools had lent money to related parties, as long as the parties had no deliberate intention to prejudice the interest of the Affected Schools and rectify measures had been taken, there was no risk of being penalised. Having considered the advice of GD Guanghe, the Company has taken measures to reverse the said transactions and restore the balances to the position before the transactions were being conducted.

(ii) Conclusion

- (I) Based on a review of the fluctuations in the balances of amounts due from/to the Affected Schools during the Period, the associated transactions between the Group and the Affected Schools appeared to be regular intercompany transactions and/or financial arrangements. These were typical among the Group and the Affected Schools, which used to be the subsidiaries of the Company until 1 September 2021.
- (II) In any case, in light of the enactment of the Implementation Regulations on 1 September 2021, related party transactions between the Group and the Affected Schools were forbidden. Upon considering the legal advice of GD Guanghe, the Company has undertaken measures to reverse the transactions that occurred between the Group and the Affected Schools during the Period. Consequently, transactions amounting to a net sum of approximately RMB177 million were reversed on or before 31 August 2022.

VIEWS OF THE IBC

The IBC has reviewed the contents of the Investigation Report and is of the view that, subject to the various limitations which the Independent Investigator encountered or observed as reported in the Investigation Report, the Independent Investigation has investigated into the Relevant Matters identified by Shinewing during the course of its review of the 2022 Interim Results to the extent that is practicable and that the content and the findings of the Independent Investigation are reasonable and acceptable.

Up to the date of this announcement, nothing was brought to the attention of the IBC with reference to the Investigation Report that would suggest any current or former Directors or senior management of the Company engaged in any fraudulent or dishonest acts with regard to the Relevant Matters that might pose a risk to shareholders and potential investors of the Company and/or damage market confidence.

Instead, the Investigation Report contained extensive discussions on background and matters surrounding the internal control issues and weaknesses of the Group, which resulted in or permitted the occurrence of the Relevant Matters.

The IBC therefore resolved that it is essential for the Company to proactively take such remedial actions as may be necessary or appropriate to safeguard the interests of the Company and its shareholders in a timely manner, including but not limited to rectifying the internal control issues to prevent the recurrence of events similar to the Relevant Matters.

INTERNAL CONTROL ISSUES IDENTIFIED

The IBC, having made due enquiries and discussions with the Independent Investigator and the IC Consultant, reasonably believes that the Relevant Matters and the Independent Investigation revealed certain internal control issues within the Group, which mainly include:

- (i) Absence of agreement management process – notable deficiencies regarding the agreement approval process were identified. The Company did not establish written policies and procedures relating to entering material agreements and other legal commitments (for example, evaluation and approval of material commitments, investments, provision of company guarantee, pledging of assets, etc.). No segregation of duties was noted in the processes of preparing and approving the agreements. In addition, key information regarding the third-party contractors and signing dates of the agreements, and important particulars concerning parties' respective obligations (for instance, scope of services and basis of determination of fees) were not properly or adequately specified in the agreements;
- (ii) Undesirable agreement execution process – the Signing Arrangements raised concern as to whether proper authorisation from the counterparties had been properly and timely obtained prior to the execution of the relevant agreements, which in turn may heighten the risk of the legality, validity and enforceability of the agreements concerned being prone to challenge;
- (iii) Inadequate management fee calculation process – there was no written procedure and policy to guide the pricing of canteen management fees. The calculation of the receivable management fee was based on the list of canteen's turnover which was provided by the finance staff of the third party contractors. No verification procedure was performed on the revenue generated from the canteen to ensure the completeness and accuracy of the data used for the calculation of the receivable management fee;

- (iv) Insufficient documentation records – no proper agreement approval record or documentation was maintained by the Company, resulted in the Company being unable to ensure that the requisite internal prior approval from the relevant management for executing material agreements having been duly obtained, which may cause the Company executing unfavourable agreements. Besides, there was a lack of meeting minutes of the Board and hence formal records for discussion during Board meetings were not available as audit trail. Without maintaining proper documentations, official proof for transactions were not available for tracking;
- (v) Inadequate related party transaction management policy – the related party transaction management policy that the Company had in place were not comprehensive and did not provide adequate guidelines for complying with the Listing Rules and relevant regulatory requirements. For instance, such policy did not include the procedures in relation to (1) establishing and maintaining a list of related parties and related parties transactions for monitoring purpose; or (2) the agreement approval process for related parties transactions;
- (vi) Failure to apprehend the latest legal and regulatory development – the Company failed to accurately understand and respond to the latest laws, regulations and policies issued by the government, resulting in the risk of non-compliance being enhanced;
- (vii) Failure to seek timely professional advice – the Company failed to seek timely professional advice from its legal, financial and/or other professional advisors prior to the entering into of material agreements and transactions, resulting in the increased risk of non-compliances or the transactions contemplated thereunder might not meet the Company’s interest;
- (viii) Absence of written policy for management of conflict of interest – there was no comprehensive written policy established for management of conflict of interest (such as procedures for mandatory regular declaration on conflict of interest by the Directors, procedures for making declarations by the staff when conflict of interest arises, and follow-up procedures for identified conflict of interest), which may result in the Company not being able to avoid and properly handle any situations of conflict of interest that may arise; and
- (ix) Incomprehensive internal control policies – while the Company had in place whistleblowing policy, shareholders’ communication policy and anti-fraud policy, these policies were not comprehensive and did not provide adequate guidelines for complying with the Listing Rules and relevant regulatory requirements (including but not limited to identifying, monitoring and disclosure of price-sensitive/inside information and other material information, notifiable transactions, and other discloseable transactions; guidelines for directors’ dealings in Company’s securities, etc.), which may result in the Company not being able to carry out its operations consistently and effectively.

RECOMMENDATIONS FROM THE IBC

Having considered the findings and recommendations set forth in the Investigation Report, the IBC has recommended the Board to adopt the findings of the Independent Investigation and has suggested the following major remedial actions (collectively the “**Recommendations**”) to the Board for actions to be taken as soon as reasonably practicable to prevent recurrence of events similar to the Relevant Matters:

- (i) the Company should implement the internal control enhancements recommended by the IC Consultant at the earliest practicable time to remediate the Company’s internal control deficiencies;
- (ii) comprehensive agreement management process (which shall govern agreement initiation, drafting, negotiation, pricing, execution, performance, auditing, reporting and renewal as well as timely consultation with external independent professional advisors) shall be established as soon as practicable and be adhered to;
- (iii) the Company shall refrain from engaging in or allowing any agreement execution process which is akin to the Signing Arrangements and the Company shall establish policy stipulating guidance for proper authorisation from counterparties;
- (iv) written legal opinions shall be obtained by the Company so as to enable it to evaluate whether the transactions identified under the Independent Investigation (for instance, (1) the receipt of the royalty income and other related party transactions during the Period subsequent to the Implementation Regulations becoming effective; and (2) the Funding Arrangement or other similar arrangement involving onshore/offshore funding arrangements) constitute non-compliance, and (if applicable) the likelihood of the Group or its officers being prosecuted, fined or penalised and the potential legal liabilities;
- (v) the Company shall work closely with its legal advisers to review all the material transactions of the Group during the Period (in particular, those transactions identified under the Independent Investigation) so as to evaluate whether there had been any incidence of non-compliance with the Listing Rules (and/or any other applicable laws and regulations), and take such appropriate remedial actions as may be recommended by its legal advisers accordingly;
- (vi) the Company shall designate a department to be responsible for monitoring projects and transactions of the Group for their compliance with the Listing Rules. As the Directors have a collective obligation to ensure Listing Rules compliance, which is a duty that cannot be entirely delegated to other parties, the Board should ensure that mechanisms are in place to enable the Company to readily identify relevant projects and transactions that have compliance requirements, so that steps can be properly taken to meet such requirements;

- (vii) the Company shall establish and strengthen an internal audit function (the “IA”), which shall comprise staff with relevant skills and expertise in internal control matters. The IA shall be tasked with the function of conducting regular review on the adequacy and effectiveness of, and compliance with, the internal control system of the Group. The IA shall be mandated by the Board with sufficient authority and resources to carry out its tasks effectively. The IA shall be accountable to the Audit Committee, and regular reporting shall be made by the internal audit function to the Audit Committee so as to enable the Audit Committee to independently review, monitor and supervise the adequacy and effectiveness of the Group’s internal controls;
- (viii) the Company shall appoint a compliance adviser or an independent professional adviser for such period as the Board may deem fit so that the Board can (1) receive periodic updates on latest legal and regulatory developments; and (2) obtain professional advises in a timely manner, to minimise the risk of non-compliances;
- (ix) regular trainings shall be arranged for its employees, including the Directors, the senior management, the operation and finance departments, to strengthen their familiarity of the Listing Rules and all applicable laws and regulations and enhance their awareness of the compliance with the internal control procedures relating to the Group’s transactions;
- (x) the Company shall put in place measures to introduce a cultural change within the Company and the Group towards greater focus on legal and regulatory compliance and observance with the internal control systems;
- (xi) the Company shall conduct an evaluation on the degree of oversights (i.e. the nature, extent, seriousness and impact of the oversights) of the individual staff involved in the Relevant Matters and take appropriate actions against such personnel accordingly (e.g. provision of necessary trainings, conduct employees’ evaluation, issue of warnings and taking of disciplinary actions);
- (xii) the Company shall assess its tax position with assistance of professional advisers in relation to the refund of the tax expenses of RMB4 million arising from the royalty income; and
- (xiii) the Company shall, having consulted its professional advisers, scrutinise its announcements, circulars, submissions published and made before to ascertain whether any further clarification(s) would be required under the Listing Rules and other applicable laws and regulations.

The Company will make further announcements to update the Shareholders and potential investors on any substantial development of the above actions as and when appropriate.

OVERALL RESPONSES FROM THE BOARD

The Board has reviewed the findings of the Investigation Report and are of the view that despite the limitations as set out in the section headed “Major Limitations of the Independent Investigation”, the Independent Investigation has been thoroughly conducted by the Independent Investigator, and has comprehensively investigated into the Relevant Matters to the extent that is practicable.

The Board concurs with the IBC that the content and findings of the Independent Investigation are reasonable and acceptable and nothing was brought to the attention of the IBC and the Board with reference to the Investigation Report that would suggest any current or former Directors or senior management of the Company engaged in any fraudulent or dishonest acts with regard to the Relevant Matters that might pose a risk to shareholders and potential investors of the Company and/or damage market confidence. The Board accepts the IBC’s recommendations in their entirety and has resolved to (i) adopt the findings of the Investigation Report and (ii) implement the recommendations of the IBC.

The Board acknowledges the remedial actions that have been taken or will be taken by the Company to improve the Group’s internal control with a view to, among other matters, preventing the recurrence of events similar to the Relevant Matters. The Board believes that (i) there is no reasonable regulatory concern regarding the integrity of the management or any individuals with substantial influence over the Company’s management and operations, which could potentially put investors at risk and undermine market confidence; and (ii) the enhanced internal control measures adopted by the Company are sufficient and effective in fulfilling the Company’s obligations and protecting its interests as per the Listing Rules.

CONTINUED SUSPENSION OF TRADING

At the request of the Company, trading in the Shares on the Stock Exchange was suspended with effect from 9:00 a.m. on 3 May 2022 due to delay in publication of the 2022 Interim Results and will remain suspended until the Company fulfils the Resumption Guidance.

By Order of the Board
China Maple Leaf Educational Systems Limited
Shu Liang Sherman Jen
Chairman and Chief Executive Officer

Hong Kong, 4 July 2023

As at the date of this announcement, the Board comprises Mr. Shu Liang Sherman Jen, Ms. Jingxia Zhang and Mr. James William Beeke as executive directors; Dr. Kem Hussain as a non-executive director; and Mr. Peter Humphrey Owen, Mr. Alan Shaver, Ms. Wai Fong Wong and Mr. King Pak Lau as independent non-executive directors.

* *For identification purposes only*