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花房集团
HUAFANG GROUP

Huafang Group Inc.
花房集团公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 3611)

INSIDE INFORMATION

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This announcement is made by Huafang Group Inc. (the “**Company**”, together with its subsidiaries, the “**Group**”) pursuant to Rule 13.09 of the Rules (the “**Listing Rules**”) Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) and the Inside Information Provisions (as defined under the Listing Rules) under Part XIVA of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong).

References are made to the announcements of the Company (i) dated June 23, 2023 in relation to the Resumption Guidance; (ii) dated February 23, 2024 in relation to the key findings of independent investigation; (iii) dated February 23, 2024 in relation to the key findings of independent internal control review; (iv) dated May 9, 2024 in relation to the Additional Resumption Guidance; and (v) dated July 2, 2024 in relation to the latest quarterly update on status of resumption (collectively, the “**Announcements**”). Unless the context requires otherwise, capitalized terms used herein shall have the same meanings as those defined in the Announcements.

I. BACKGROUND

As disclosed in the Company’s announcement dated March 31, 2023, the Company is unable to publish its 2022 Audited Annual Results by March 31, 2023 because the Company needs additional time to provide relevant documents required by the Company’s auditor for certain bank accounts which have been frozen. Accordingly, trading in the shares of the Company on the Stock Exchange has been suspended with effect from 9:00 a.m. on April 3, 2023 due to the delay in publication of the 2022 Audited Annual Results.

As disclosed in the announcement of the Company dated April 25, 2023, certain authorities in the People’s Republic of China initiated an investigation on an investee company (the “**Investee Company**”) in which the Group holds 25% equity interest (the “**Criminal Case**”), which involves the Frozen Accounts. Please refer to the announcement by the Company dated February 23, 2024 in relation to the key findings of the independent investigation for details of the Criminal Case.

As disclosed in the Company’s announcement dated July 25, 2023, the Group tendered detained funds pending final judgment (待結案扣押款) of approximately RMB155 million to the relevant government authority. As of July 25, 2023, all Frozen Accounts had been released and available for daily business operations.

On August 31, 2023, the Company appointed AOGB as the independent investigator to conduct an independent investigation to assess the impact of the incidents of the Frozen Accounts and the Criminal Case on the Company’s business operation and financial position (the “**Independent Investigation**”). AOGB issued the Investigation Report on February 19, 2024.

Further information on the key findings of the Independent Investigation are set out in the Company’s announcement dated February 23, 2024.

On May 6, 2024, the Stock Exchange imposed the Additional Resumption Guidance, pursuant to which the Company is required to demonstrate that there is no reasonable regulatory concern about the integrity, competence or character of the Group’s management and/or any persons with substantial influence over the Company’s management and operations, which may pose a risk to investor and damage market confidence. Accordingly, the Company appointed AOGB as the forensic investigator (the “**Forensic Investigator**”) to conduct the Forensic Investigation.

On September 17, 2024, the Forensic Investigator issued the report of the Forensic Investigation (the “**Forensic Investigation Report**”).

Based on the findings in the Forensic Investigation Report, the Forensic Investigator recommended certain Improvement Measures (as defined and detailed in Section IV below). The Company engaged the Internal Control Consultant to carry out a supplemental internal control review in response to such recommendations (the “**Supplemental Internal Control Review**”). On September 18, 2024, the Internal Control Consultant issued a report of the supplemental internal control review (the “**Supplemental Internal Control Review Report**”).

II. SCOPE OF THE FORENSIC INVESTIGATION

The Forensic Investigator conducted the Forensic Investigation into the Group's internal and external communications regarding the Pre-IPO Frozen Accounts (as defined in paragraph A of Section III below) to assess whether the Company fulfills the Additional Resumption Guidance.

For the purpose of the Forensic Investigation, the Forensic Investigator performed the following independent procedures, including but not limited:

1. interviewed the Directors and the Management;
2. obtained and reviewed communication records or other supporting documents (if any) provided by the Group's current and resigned employees;
3. interviewed the joint sponsors for the Company's listing (the "**Listing**") and obtained and reviewed communication records or other supporting documents (if any) between the Group and the external parties; and
4. conducted electronic data analysis, such as obtaining the electronic devices of key personnel and reviewing electronic evidence such as data from such key personnel's emails and local files.

III. SUMMARY OF THE KEY FINDINGS OF THE FORENSIC INVESTIGATION

A. The Frozen Accounts

According to the Forensic Investigation Report, the Forensic Investigator observed that:

- (a) on August 22, 2022, the Company became aware that one of its Alipay account was frozen on August 18, 2022;
- (b) on October 14, 2022, the Company became aware that apart from the Alipay account mentioned in (a) above, there were additionally four Alipay accounts being frozen since August 18, 2022;
- (c) in the evening of November 30, 2022, the Company became aware that 20 Alipay accounts were frozen on November 30, 2022; and
- (d) on March 17, 2023 and March 22, 2023, the Company became aware that a further 25 Alipay accounts and a bank account, respectively, were frozen on March 17, 2023 and March 22, 2023.

The frozen Alipay accounts mentioned in (a), (b) and (c) above are collectively referred to as the “**Pre-IPO Frozen Accounts**”. The Pre-IPO Frozen Accounts and the frozen Alipay accounts and bank account mentioned in (d) above are collectively referred to as the “**Frozen Accounts**”.

As of July 25, 2023, all Frozen Accounts had been released and available for daily business operations.

B. The Then Management Team’s Reaction to the Freezing of the Frozen Accounts

According to the Forensic Investigation Report, upon becoming aware of the freezing of the Frozen Accounts, the then management team of the Company (including Ms. Yu Dan (Chief Executive Officer and an executive Director) (“**Ms. Yu**”)) (the “**Then Management Team**”) took steps to communicate with the relevant authority regarding the circumstances leading to the freezing of the Frozen Accounts. The Then Management Team also carried out a self-inspection to ascertain if the Group was involved in any illegal or unusual business circumstances, and conducted an analysis on the impact of the Frozen Accounts on the Group.

Having considered that (a) the freezing of the Frozen Accounts was unrelated to the Group’s products and operations; (b) the freezing was temporarily to facilitate an on-going investigation (the “**Investigation**”) and the Frozen Accounts would be unfrozen once the relevant authority completed the evidence collection process; (c) no illegal circumstances were found after completion of the self-inspection on the business and operations of the Group; (d) the businesses of the Group continued to operate normally and had not been materially impacted by the freezing of the Frozen Accounts; and (e) the cash balance of the Pre-IPO Frozen Accounts was relatively immaterial compared to the then available cash balance of the Group at each relevant point of time, the Then Management Team considered the freezing of the Pre-IPO Frozen Accounts to be of operational nature and the Pre-IPO Frozen Accounts were expected to be unfrozen shortly. Hence, it was considered that the freezing of the Pre-IPO Frozen Accounts was not material information which warranted disclosure to other members of the Board (the “**Other Directors**”) and professional parties involved in the Listing (apart from the ex-auditors of the Company).

On March 17, 2023, the Then Management Team became aware that the Investigation became the Criminal Case and took actions to report the freezing of the Frozen Accounts to the Other Directors.

C. Key Observations by the Forensic Investigator

1. The Forensic Investigator observed that, prior to the Listing, Ms. Yu became aware of the Pre-IPO Frozen Accounts and had made a judgement regarding the Pre-IPO Frozen Accounts based on the information available to her at the relevant time. The Forensic Investigator did not find any inconsistency between the information possessed by Ms. Yu at the relevant time and the factual basis of her judgment, or any evidence which indicated that Ms. Yu became aware that the Pre-IPO Frozen Accounts should have been discloseable but chose not to disclose it.
2. Prior to the Listing, based on the information available to Ms. Yu and the Then Management Team at the relevant time, they made a judgement that the Pre-IPO Frozen Accounts did not constitute information that should have been discloseable. There is no evidence which indicates that any of them has, collectively or individually, deliberately or negligently, concealed the Pre-IPO Frozen Accounts from the Other Directors, professional parties involved in the Listing or relevant regulatory authorities (including the Stock Exchange).
3. The Other Directors first became aware of the Frozen Accounts in around mid to late March 2023. While the Other Directors do not participate in the Group's daily operations, they review and vote on matters submitted by the management to the Board (or its subordinate committees), supervise the Group's risk management and internal control systems, supervise the timeliness and accuracy of the Company's information disclosure, and maintain communication with the Company's management to understand the operation and financial position of the Group, any material matters which will affect the operations and financial position of the Group, and to raise appropriate questions regarding the Group's operations and financial position at material times. The findings of the Forensic Investigation did not show that any of the Other Directors had been made aware of, or reminded of, the Pre-IPO Frozen Accounts and its importance prior to the Listing.
4. The Forensic Investigator did not observe that prior to the Listing, any of the Other Directors was aware of the Pre-IPO Frozen Accounts but deliberately or negligently concealed the Pre-IPO Frozen Accounts from the professional parties involved in the Listing or relevant regulatory authorities (including the Stock Exchange).
5. The Forensic Investigator has (a) read the prospectus issued by the Company on November 30, 2022, the PRC legal opinion dated November 30, 2022, which did not contain reference to the Pre-IPO Frozen Accounts or any on-going investigation; (b) interviewed Ms. Yu and an ex-employee of the Group who mentioned that they did not consider it necessary to report the freezing of the Pre-IPO Frozen Accounts to the Board; and (c) reviewed the email exchanges with the Other Directors before the Listing (mainly meeting agenda and minutes), which did not contain any references to the freezing of the Pre-IPO Frozen Accounts or any information that would bring to the attention of the Other Directors of the freezing of the Pre-IPO Frozen Accounts.

IV. IMPROVEMENT MEASURES RECOMMENDED BY THE FORENSIC INVESTIGATOR

The Forensic Investigator recommended the Company to adopt the following improvement measures (the “**Improvement Measures**”):

1. the Group shall further enhance its corporate governance, clearly set out the authorization and communication mechanism between the Board and the management to ensure timely communication of material information;
2. taking into consideration its business characteristics and past experience, the Group shall define parameters for classifying matters into abnormal, major or important matters and enhance and expand the assessment parameters to include factors, such as the nature of the matter, time required to obtain further information, monetary value involved, whether there are any other key milestone events (such as new product launch, etc.), such that relevant matter could be reported to the Board for its comprehensive consideration in a timely manner. Professional advice should also be given more weight in the decision making process;
3. the Group shall analyze and assess each important matter from different angles and in a collective manner. In particular, where such matter involves multi-departments, all relevant personnel should be duly informed to ensure there is efficient and effective communication both internally and externally to avoid any decision being affected by miscommunication;
4. all discussions among the Group’s management should be properly documented, such records should include all factors considered, the identities of the participants, their opinions and basis for such opinion (including opinions and basis of participants who have different views) and conclusions of such discussion; and
5. when enquiring the management on post-period matters or the status of transactions, the Board should, taking into account the Group’s business and industry risks, raise questions with a view to identifying issues (if any) instead of asking procedural questions.

V. MAJOR LIMITATIONS OF THE FORENSIC INVESTIGATION

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

1. the Forensic Investigator was unable to conduct interviews with (a) the engagement partner responsible for the Group's audit during the listing process who did not respond to the invitation for interview; (b) certain key personnel of the Investee Company and certain ex-employees of the Group who either was subject to criminal compulsory measures or did not respond to the invitation for interview;
2. the Forensic Investigator was unable to obtain and review the emails of certain ex-employees as their computers have been reset and the mailboxes have been cleared from the server upon their departure; and
3. the Forensic Investigator was unable to perform electronic data analysis on a real-time communication software used by the Group as the Group's subscription of such software has been terminated in April 2023.

VI. VIEWS OF THE AUDIT COMMITTEE AND THE BOARD ON THE FORENSIC INVESTIGATION

The Audit Committee and the Board have reviewed and accepted the content and findings of the Forensic Investigation in the Forensic Investigation Report. The Audit Committee and the Board recommended that the Group should adopt and implement the Improvement Measures.

The Audit Committee has considered the forensic investigation procedures carried out by the Forensic Investigator, and the limitations encountered by the Forensic Investigator. After reviewing the Forensic Investigation Report, the Audit Committee accepted the key findings of the Forensic Investigation in the Forensic Investigation Report, which covered (i) the extent of involvement of each of Ms. Yu and the Other Directors in the Pre-IPO Frozen Accounts, including when and how each of them became aware of the Pre-IPO Frozen Accounts and the actions taken by each of them upon finding out the accounts were frozen; (ii) the facts and circumstances leading to, and the reason and basis of Ms. Yu and the Other Directors not disclosing the Pre-IPO Frozen Accounts to the relevant parties and in the prospectus issued by the Company on November 30, 2022; and (iii) whether there were circumstances or information that should have reasonably put the Other Directors on notice or enquiry warranting follow up on any potential irregularities.

The Audit Committee considered (i) the Forensic Investigation was conducted based on multiple sources of information available, including review of internal documents and data, interviews with all Directors and relevant employees of the Company who were still contactable, and electronic forensic data discovery and reviews; and (ii) the key findings of the Forensic Investigator as set out in “III. SUMMARY OF THE KEY FINDINGS OF THE FORENSIC INVESTIGATION — C. Key observations by the Forensic Investigator” in this announcement. Based on the above, the Audit Committee considered that the scope of the Forensic Investigation by the Forensic Investigator is adequate.

The Board shared the views of the Audit Committee towards the findings and scope of the Forensic Investigation Report.

VII. THE SUPPLEMENTAL INTERNAL CONTROL REVIEW

A. Scope of the Supplemental Internal Control Review

For the purposes of reviewing the internal control systems of the Group in relation to the Improvement Measures (the “**Relevant Internal Control System**”), the following is the scope of the Supplemental Internal Control Review conducted by the Internal Control Consultant:

1. review and discuss with the Management the related policies and procedures in relation to the Relevant Internal Control System to understand how the Relevant Internal Control System was carried out during the period from August 18, 2022 to March 31, 2023 (the “**Review Period**”);
2. peruse the policies and procedures, the meeting minutes, reports and organization chart and other support documents, and conduct walk-through testing;
3. report findings on major weaknesses and deficiencies on the design and implementation of the Relevant Internal Control System identified by the Internal Control Consultant;
4. recommend rectification measures with respect to the weaknesses and deficiencies identified in the review process; and
5. carry out follow-up review after the Group has carried out rectification measures and issue the final report upon completion of the follow-up review.

B. Key Findings of the Supplemental Internal Control Review

The key findings of the Internal Control Review, corresponding recommendations for rectification and the response of the Management are summarized as follows:

Key findings	Recommendation	The Management’s response and follow-up results
<p>During the Review Period, the scope of major matters to be reported to the Board is not clearly defined.</p>	<p>There should be guidance on matters to be reported to the Board by the Management, including defining matters to be reported (with defined parameter for classifying abnormal/major/important matters, nature of the matter, time required to obtain further information, monetary value involved, number of departments involved, whether there are any other key milestone events (such as listing, new product launch), etc. for assessment), reporting channel, information collection and analysis and personnel involved in the reporting process.</p>	<p>The Management agreed to the recommendation and enhanced, amended and supplemented the relevant internal control policies, which became effective on September 6, 2024 upon approval by the Board.</p>
<p>During the Review Period, there was no comprehensive cross-departmental discussion and consideration in respect of material matters, and most of the communications in relation to the Frozen Accounts were carried out orally and not properly documented.</p>	<p>Important matters shall be analyzed and assessed from different angles and in a collective manner. In particular, where such matter involves multi-departments, all relevant personnel should be duly informed to ensure there is efficient and effective communication both internally and externally to avoid any decision being affected by miscommunication.</p> <p>All discussions should be properly documented, such records should include all factors considered, the identities of the participants, their opinions and basis for such opinion (including opinions and basis of participants who have different views) and conclusions of such discussion.</p>	<p>The Management agreed to the recommendation and enhanced, amended and supplemented the relevant internal control policies, which became effective on September 6, 2024 upon approval by the Board.</p>

Key findings	Recommendation	The Management's response and follow-up results
During the Review Period, clear guidance has not been included in the relevant information provided to the Board to enable it to undertake further enquiries and to assess whether any financial and compliance disclosure is required.	<p>Periodic information package to be sent to the Board by the Management shall include: defined recipients of such information and reporting time, update information (including financial statements or analysis of major/important operational changes).</p> <p>When approving financial reports for external publication, the Board should make further enquiries, if necessary, on the basis of the information available to them.</p>	The Management agreed to the recommendation and enhanced, amended and supplemented the relevant internal control policies, which became effective on September 6, 2024 upon approval by the Board.

VIII. VIEWS OF THE AUDIT COMMITTEE AND THE BOARD ON THE SUPPLEMENTAL INTERNAL CONTROL REVIEW

The Audit Committee and the Board noted that, in response to the internal control deficiencies identified by the Forensic Investigator in the Forensic Investigation Report, the Company has engaged the Internal Control Consultant to carry out the Supplemental Internal Control Review, and the Group has implemented all the remedial actions recommended by the Internal Control Consultant. It was also noted that the Internal Control Consultant has performed follow-up review on the Relevant Internal Control System, and is satisfied that the Group has adopted the remedial actions recommended to address the deficiencies identified.

Having considered the Supplemental Internal Control Review and the recommendations and findings by the Internal Control Consultant, the Audit Committee and the Board are of the view that the remedial actions taken by the Group are adequate and sufficient to address the internal control deficiencies identified, and that the Group has in place adequate internal control and procedures to meet its obligations under the Listing Rules.

IX. CONTINUED SUSPENSION OF TRADING

At the request of the Company, trading in the shares of the Company on the Stock Exchange was suspended with effect from 9:00 a.m. on April 3, 2023 pending the publication of the 2022 Audited Annual Results, and will remain suspended until the Company fulfils the Resumption Guidance and any supplement or modification thereto. The Company will publish further announcement(s) to inform the shareholders of the Company of its progress in complying with the Resumption Guidance as and when appropriate, as well as quarterly updates on its development pursuant to Rule 13.24A of the Listing Rules.

Shareholders and potential investors of the Company should exercise caution when dealing in the securities of the Company.

By order of the Board
Huafang Group Inc.
花房集团公司
Mr. ZHOU Hongyi
Chairman

Hong Kong, September 19, 2024

As at the date of this announcement, the Board comprises Ms. YU Dan as executive director; Mr. ZHOU Hongyi, Mr. CHEN Shengmin and Mr. ZHAO Dan as non-executive directors; and Mr. CHEN Weiguang, Mr. LI Bing and Ms. QIAN Aimin as independent non-executive directors.