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自然美

NATURAL BEAUTY

Natural Beauty Bio-Technology Limited

自然美生物科技有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock code: 00157)

INSIDE INFORMATION

KEY FINDINGS OF INTERNAL CONTROL REVIEW

This announcement is made by Natural Beauty Bio-Technology Limited (the “**Company**”, and together with its subsidiaries, the “**Group**”) pursuant to Rule 13.09 of the Rules Governing the Listing of Securities (the “**Listing Rules**”) 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).

Reference is made to (i) the announcements of the Company dated 24 March 2020, 29 April 2020, 24 June 2020, 21 July 2020, 27 July 2020 and 23 September 2020 in relation to, amongst others, an investigation on certain audit findings raised by the Company’s previous auditors (the “**Forensic Review**”); (ii) the announcements of the Company dated 21 May 2020 and 14 August 2020 in relation to the conditions for the resumption of trading in the shares of the Company (the “**Resumption Conditions**”); (iii) the announcement of the Company dated 14 August 2020 in relation to the appointment of the auditors of the Company; (iv) the announcement of the Company dated 25 August 2020 in relation to, among others, the appointment of the internal control consultant; (v) the announcement of the Company dated 20 November 2020 in relation to the key findings of Additional Forensic Review; (vi) the announcement and the supplemental announcement of the Company dated 30 November 2020 in relation to the audited annual results of the Group for the year ended 31 December 2019; and (vii) the announcement of the Company dated 30 November 2020 in relation to the Auditors’ letter to the Audit Committee. Unless otherwise stated, capitalised terms used herein shall have the same meanings as those defined in the announcement of the Company dated 20 November 2020 (the “**Announcement**”).

OBJECTIVE OF THE INTERNAL CONTROL REVIEW

As disclosed in the announcement of the Company dated 14 August 2020, one of the Resumption Conditions is for the Company to conduct an independent internal control review and demonstrate that the Company has in place adequate internal control and procedures that address the concerns identified in the forensic review referred to in the Company's announcement dated 21 July 2020 and ensure the Company to comply with the Listing Rules.

To assist the Company in fulfilling this condition, the Company engaged SHINEWING Risk Services Limited ("**Shinewing**") as its internal control consultant to conduct a review of the internal control systems and procedures of the Group in response to the concerns identified in the Forensic Review and the Additional Forensic Review (the "**Internal Control Review**").

As disclosed in the Company's announcements dated 21 July 2020 and 20 November 2020, the key findings of the Forensic Review and the Additional Forensic Review pertain to the following subject matters ("**Subject Matters**"):

Subject Matter	Key findings
Subject Matter 1	Sales spike relating to four individual distributors and arrangement on goods exchange quota granted to distributors
Subject Matter 2	Concerns over how certain individual distributors and customers settled their payments by employees or multiple payers
Subject Matter 3	Some sales did not appear to be supported by third party evidence of delivery
Subject Matter 4	Fictitious sales allegations
Subject Matter 5	Accounts receivables of the major customers as of 31 May 2020
Subject Matter 6	Revenue recognition appears to be inconsistent with the Company's accounting policy
Subject Matter 7	Allegation of channel stuffing prior to 2019

The Internal Control Review mainly focused on the Company's internal control pertaining to the above Subject Matters and consisted of two phases:

- (a) the objectives of phase one of the Internal Control Review were to (i) independently review the internal control system as established by the Company, its adequacy and integrity vis-à-vis the objectives served; (ii) make appropriate recommendations; and (iii) enable the Company to enhance the internal control in respect of the concerns identified in the Forensic Review and Additional Forensic Review;
- (b) the main objective of phase two of the Internal Control Review was to assess the remediation status of the deficiencies identified during phase one of the Internal Control Review and the concerns identified in the Forensic Review and Additional Forensic Review.

OVERVIEW OF RESULTS OF THE INTERNAL CONTROL REVIEW

Set forth below is an overview of the results of the Internal Control Review and the remediation status of the internal control deficiencies as at 30 November 2020:

Selected Process	Relevant Subject Matters	Remediation status as at 30 November 2020
General	–	Remediated
Sales proceeds collection	Subject Matter 2	Remediated
Accounts receivable management	Subject Matter 5	Remediated
Customer and sale order management	Subject Matter 1 & Subject Matter 7	Remediated
Management of franchise stores	Subject Matter 4	Remediated
Goods delivery	Subject Matter 3 & Subject Matter 7	Remediated
Revenue recognition	Subject Matter 6 & Subject Matter 7	Remediated

ENHANCED INTERNAL CONTROL MEASURES

In response to the Subject Matters identified in the Forensic Review and Additional Forensic Review, Shinewing noted that the Company has taken the following enhanced internal control measures on both entity level and activity level.

Summary of entity level controls

Entity level controls

Strengthening of internal control and supervision

Key enhanced internal control measures

Appointment of external directors

In order to strengthen the Company's internal control and the supervision of the board of directors in the mainland subsidiaries, the Company has appointed additional external directors to the board of directors in the mainland subsidiaries on 30 October 2020.

Increase in frequency in Board meetings

The frequency of Board meetings has been increased to be held on a quarterly basis to strengthen the controls over the Company's operations and internal audits.

Enhanced internal audit monitoring

The Company has amended its internal audit plan to address all the findings identified during annual audit for the financial year of 2019, the Forensic Review and the Additional Forensic Review. Findings with significant impact have been included in the scope of the 2020 internal audit review; while the remaining less significant issues will be covered in phases in 2021. Findings of internal audit reports will be submitted to the CEO and Board for their review and discussion on a quarterly basis.

Enhanced Training

Training has been provided to all newly joined employees. In addition to the regular training, information regarding the findings identified during the annual audit for the financial year of 2019, the Forensic Review and the Additional Forensic Review are also highlighted to the staff members as key points to note.

Annual refresher training plan has also been formulated to raise the awareness of the existing staff.

Restructuring of sales team and establishment of new authorised dealer team

The Company has restructured the current sales team structure, by splitting the sales team in the mainland China into 5 sales regions and a specialised team for authorised dealers has been formed to enhance the supervision of sales operations.

Setting up customers reporting channels

In order to regulate the business behaviour of employees, a CEO hotline has been set up for franchisees or distributors to report employees' misconducts such as dishonesty and misrepresentation.

Questionnaires are also designed to gather information and feedbacks from customers. Customers can access the questionnaire by scanning the QR-code or website created by the Company.

Enhancement of standard operating procedures

The Company has implemented various operating procedures and remedial actions to further enhance its controls in sales proceeds collection, distributor management (with controls on goods exchange quota granted to distributors), goods delivery and revenue recognition.

The Company has issued notices, internal policies and an updated employee handbook. The latest policies and procedures have been circulated to all relevant parties.

Summary of activity level controls

Specific to each Subject Matter, the Company has implemented the following remedial and preventive enhanced internal control measures:

Subject Matter

Key enhanced internal control measures

Subject Matter 1:

Order Management

Sales spike relating to four individual distributors and arrangement on goods exchange quota granted to distributors

An application programme has been introduced to record the confirmation of sale orders from customers since July 2020. Customers are required to verify the sale order through their own user accounts.

The relevant policies and procedures were established to document the account re-activation and approval procedures.

Goods exchange management

The Company has redrafted the Authorised Dealer Agreement which includes the terms and condition for goods exchange.

The goods exchange processes have also been included in the relevant policies and procedures.

The finance department is required to manage and monitor the goods exchange quota. Email confirmations have been sent to authorised dealers periodically to reconcile any outstanding goods exchange quota which has not been redeemed.

Furthermore, an application programme will be launched in 2021 to allow the authorised dealers to review the statement of transactions and the goods exchange quota.

Subject Matter 2:

Concern over how certain individual distributors and customers settled their payment by employees or multiple payers

The Company has stopped accepting payment from WeChat Pay and has only allowed Alipay and card payments (which could verify the payer's identity) since late June 2020.

The Company has introduced point-of-sale terminal from UnionPay, which allows backend identity verification of the payers.

The Company also issued a notice to all customers in November 2020, requiring all payments to include relevant details such as customer's name and customer's code.

The finance department has checked and maintained the details of payment records of its sales receipts for payer identification.

Relevant policies and procedures have also been established to govern the procedures regarding payment on behalf of the customers and prohibit employees from paying on behalf of customers.

Subject Matter 3:

Some sales did not appear to be supported by third party evidence of delivery

The Company has signed a Logistic Agreement with a new logistic service provider. Relevant logistic records including sales order number, delivery tracking number, recipient, delivery address, date of delivery are kept and provided to the Company as an audit trail.

The tracking records or the Delivery Notes have been properly maintained as supporting documents for the goods delivery.

In addition, logistics staff is required to timely communicate with the customers and confirm goods delivery status. Any discrepancies noted should be promptly investigated and reported to the management.

Besides, the abovementioned processes have been included in relevant policies and procedures.

Subject Matter 4:

Declaration on conflict of interests

Fictitious sales allegations

All employees and customers are required to declare their conflicts of interests annually.

The declarations of both franchisees and employees and application forms of franchisees have been properly filled in.

The enhanced process has also been included in the relevant policies and procedures.

Review of existing franchisee

The Company has updated its evaluation criteria, and the assessment results have been recorded for management's review and approval.

Subject Matter 5:

Accounts Receivables of the Major Customers as of 31 May 2020

An application programme has been launched in November 2020 to assist the finance department in performing the receivables reconciliation with each franchisee. The franchisee reviews the details of the outstanding receivables and confirms the reconciliation through the application programme on a monthly basis.

The enhanced processes have also been included in relevant policies and procedures.

Subject Matter 6:

Revenue recognition appears to be inconsistent with the Company's accounting policy

The finance department has compiled the information of the orders which were delivered, but not received by the customers at the end of each month.

The Company has maintained the delivery notes and tracking records for the finance department to check if there are any cut-off issue.

If required, the finance department will prepare corresponding accounting adjustments to the finance records.

The enhanced processes have also been included in the relevant policies and procedures.

Subject Matter 7: The enhanced internal control measures adopted for Subject Matter 1, Subject Matter 3 and Subject Matter 6 are also applicable to Subject Matter 7.

Allegation of channel stuffing prior to 2019

In addition, the warehouse team is required to check the accuracy of products against the information stated on packing list upon goods dispatching. If a problem is identified, the goods will not be dispatched for delivery.

RESULTS OF THE INTERNAL CONTROL REVIEW

During the Internal Control Review, Shinewing has performed testing on the enhanced internal control processes, and no irregularities were noted. As the internal control deficiencies identified in the Internal Control Review have been fully remediated, Shinewing is of the view that the Company has put in place adequate internal control and procedures to address the concerns identified in the Forensic Review and the Additional Forensic Review, and meet its obligations under the Listing Rules.

In addition, on 27 November 2020, the Auditors had sent a letter to the Audit Committee setting out certain internal control deficiencies identified during the Auditors' audit. In response, the Audit Committee had requested Shinewing to assess the internal control deficiencies as raised by the Auditors. On 2 December 2020, Shinewing confirmed to the Audit Committee that the Internal Control Review has covered all the internal control deficiencies as identified by the Auditors in its letter, and that the remedial measures implemented by the Company are sufficient and adequate to address the Auditors' concerns in its letter.

VIEWS OF THE AUDIT COMMITTEE AND THE BOARD OF DIRECTORS

Having considered the results of the Internal Control Review, the Audit Committee and the Board are of the view that the remedial measures implemented by the Company are sufficient and adequate to address the concerns identified by the Auditors, in the Forensic Review and the Additional Forensic Review, and meet its obligations under the Listing Rules.

CONTINUED SUSPENSION OF TRADING

Trading in the Shares on the Stock Exchange has been suspended at the request of the Company since 9:00 a.m. on 25 March 2020 and will remain suspended until further notice. Shareholders and potential investors of the Company are advised to exercise caution when dealing in the securities of the Company.

By order of the Board
Natural Beauty Bio-Technology Limited
LEI Chien
Chairperson

Hong Kong, 2 December 2020

As at the date of this announcement, the Board comprises Dr. Lei Chien and Mr. Pan Yi-Fan as executive directors; Ms. Lu Yu-Min, Ms. Lin Shu-Hua and Mr. Chen Shou-Huang as non-executive directors; and Mr. Chen Ruey-Long, Mr. Lu Chi-Chant and Mr. Yang Shih-Chien as independent non-executive directors.