

BEST WORLD INTERNATIONAL LIMITED

Company Registration No. 199006030Z

INDEPENDENT REVIEW – ISSUE OF FINAL REPORT

The Board of Directors of the Company (the “**Board**” or “**Directors**”) of Best World International Limited (the “**Company**” and together with its subsidiaries, the “**Group**”) refers to:

- (a) the Company’s announcements dated 23 February 2019, 19 March 2019, 15 July 2019, 12 December 2019 and 14 February 2020 relating to the conduct by PricewaterhouseCoopers Advisory Services Pte. Ltd. (the “**Independent Accountant**”) of an independent review of the Export Model and the Franchise Model adopted by the Group in China (the “**Independent Review**”);
- (b) the Notice of Compliance issued by Singapore Exchange Regulation Pte Ltd (“**SGX RegCo**”) to the Company on 13 May 2019 (the “**Notice of Compliance**”); and
- (c) the Company’s announcement dated 22 March 2020 relating to the interim update issued by the Independent Accountant on the Independent Review.

The Independent Accountant has completed the Independent Review and set out its findings in a final report (the “**Report**”) that has been issued to the audit committee of the Company (the “**AC**”) on 23 July 2020. During the course of the Independent Review, the Independent Accountant reported its findings solely to SGX RegCo. An executive summary of the Independent Report (the “**Executive Summary**”) prepared by the Independent Accountant is annexed to this announcement. The scope of the Independent Review is set out in paragraphs 1 to 3 of the Executive Summary. The Company’s shareholders (“**Shareholders**”) are advised to read this announcement in conjunction with the Executive Summary. The responses of the Company’s management (“**Management**”) to the key findings of the Independent Accountant have been incorporated by the Independent Accountant in the Executive Summary.

The Board has noted the findings of the Independent Accountant and Management’s responses. The Board has also received preliminary legal advice on the issues that have been identified in paragraphs 30, 56 and 90 to 95 of the Executive Summary and the potential legal risks that may be faced by the Group. Many of the issues raised in the Report are historical issues that would have been resolved with the completion of the transitional arrangements related to the Group’s transition from the Export Model to the Franchise Model from June 2018 to June 2019. Accordingly, the Board intends to focus on undertaking an assessment of the Group’s existing corporate governance, internal controls and risk management to ensure that any irregularities from past practices will not arise in the future. The AC will work collectively with the Executive Directors as a Board to formulate an action plan to mitigate any ongoing legal, regulatory and compliance risks as indicated in the Report.

The Notice of Compliance required the Company to obtain an independent legal opinion on the legality of the Group’s sales and distribution model under the Franchise Model (the “**Legal Opinion**”). Accordingly, the Company engaged Merits and Tree (Beijing) Law Office (“**M&T**”), an independent law firm in China, to provide the Legal Opinion.

Action Plan

The Board believes that strong corporate governance is important for safeguarding the Group's assets, ensuring reliable financial reporting and achieving operational efficiency. As announced by the Company on 23 February 2019, in conjunction with the Group's transition from the Export Model to the Franchise Model, the Company had engaged a third party internal controls consultant firm to review and make recommendations on the Group's internal controls policies with respect to entity-level controls, which included financial and accounting procedures. All of these recommendations had been substantially implemented by the Group by January 2019. To address the specific issues identified by the Independent Accountant in the Report which were not covered in the earlier internal controls review, the Board plans to engage an external consulting firm to work with its legal advisers to consider the recommendations of the Independent Accountant and undertake a diagnostic review of the Group's existing corporate governance, legal and compliance processes, as well as the accounting practices highlighted as an area of concern in the Report. In addition, as recommended by the Independent Accountant, the Board, in due course, will appoint a senior compliance officer to develop and implement any agreed remedial actions and to take all necessary steps to oversee the compliance function, who will report directly to the AC.

The Board would like to reassure Shareholders that all necessary actions to safeguard the interests of Shareholders and the Group will continue to be taken. As disclosed in the Company's Annual Report for the financial year ended 31 December ("FY") 2018, the Group is strategically focused on gaining a stronger foothold in China over the next three (3) to five (5) years and to secure avenues of higher growth for the Group.

As previously disclosed in the Company's announcement on 23 February 2019, the Group had originally considered a direct transition from the previous Export Model to a direct selling model in China. However, due to the higher barriers to entry of the direct selling industry in China, such as requirements to apply for the expansion of the coverage of the Group's existing direct selling license and establish service outlets in every district of every city in which the Group's products are distributed, the Group determined that a transition to the Franchise Model would permit a more seamless integration with the Group's distribution network under the earlier Export Model. As the Group had little experience operating in the China market at the time, this strategy would allow the Group to continue expanding its operations and building brand equity for its products in the China market more cost effectively and better manage the accompanying expansion risks.

To continue growing the demand for the Group's products in China, the Board is pleased to announce that the Group plans to eventually transition from the current Franchise Model to direct selling, in line with the Group's long term strategy. With the encouraging growth of the Group's China business, increasing brand recognition in China, and the Group's improved financial performance since the transition to the Franchise Model, the Group believes that it is in a better position at this time to pivot its China operations and transition to direct selling. As at the date of this announcement, the Group is formulating its strategy for the eventual transition to direct selling in China, and will make further announcement(s) as and when there are any material developments on this matter.

Key Objectives of the Independent Review

The Independent Accountant was engaged to perform an independent review of BW Changsha with several key objectives. For the convenience of Shareholders, the table below sets out a brief summary of the findings of the Independent Accountant in relation to the key objectives of the Independent Review. Further details on the Independent Accountant's findings are set out in the section entitled "Key Findings of the Independent Review" below and the Executive Summary annexed to this announcement. The work and findings of the Independent Accountant in the Report are based on the documents that have been made available to it and is subject to the limitations set out in paragraph 97 of the Executive Summary.

Objectives	Brief summary of findings
To verify the existence of the Franchisees as at 31 December 2018.	<p>The Independent Accountant selected eight (8) Franchisees and performed site visits to verify the existence of each Franchisee's physical shop front, which were arranged by BW Changsha. The Independent Accountant also performed four (4) additional surprise visits to other Franchisees.</p> <p>Please refer to paragraph 3.1 of the section entitled "Key Findings of the Independent Review" below and paragraphs 57 to 60 of the Executive Summary.</p>
To validate the sales to the significant Franchisees (by sales value).	<p>The Independent Accountant did not note any significant exceptions based on the work performed on the samples selected. The Independent Accountant traced the sales and movement of goods from the Company to BW Changsha during the Franchise Model period to third party documents such as bills of lading on a sampling basis, and payments for these goods to the bank statements of the Company and BW Changsha. The Independent Accountant also further performed a throughput analysis of the DR's Secret Stock Keeping Unit ("SKU")¹ from the quantity of raw materials purchased by the Company to the quantity of finished goods sold to BW Changsha.</p> <p>In respect of BW Changsha's sales to significant Franchisees, the Independent Accountant was able to trace such sales recorded in BW Changsha's financials on a sampling basis for the period from 1 June 2018 to 31 December 2018 to underlying invoices, delivery instructions, third party warehouse records and confirmations from third-party logistics providers.</p> <p>Based on the Independent Accountant's work, the following exceptions were noted:</p>

¹ Throughput analysis was performed only on DR's Secret SKU as these constitute the majority of sales in China.

	<p>(a) potential sales cut-off issue for goods sold which remained undelivered as at 31 December 2018; and</p> <p>(b) potential understatement of BW Changsha’s sales and certain related expenses.</p> <p>Please refer to paragraph 3.2 of the section entitled “Key Findings of the Independent Review” below and paragraphs 65 to 71 of the Executive Summary.</p>
To validate the cash received from the sales to the significant Franchisees.	<p>The Independent Accountant independently obtained the physical bank statements of BW Changsha and agreed the cash balance as at 31 December 2018 to the financial records of BW Changsha. The Independent Accountant also analysed the cash movement of BW Changsha to understand the significant movements from 1 June 2018 to 31 December 2018.</p> <p>Please refer to paragraphs 65 and 72 to 75 of the Executive Summary.</p>
To establish the facts and circumstances surrounding the establishment, appointment and business relationship with the primary import agent.	<p>An account of the facts and circumstances surrounding the establishment, appointment and business relationship with the primary import agent is set out in paragraph 7 of the Executive Summary.</p>
To verify the sales to the primary import agent and other import agents used by the Group in the China market, if any, for the period from FY2015 to FY2018 under the Export Model, and ascertain if these transactions were on normal commercial terms and conducted at an arm’s length basis.	<p>In respect of the Group’s sales to import agents² under the Export Model, the Independent Accountant did not note any significant exceptions based on the work performed on the samples selected. The Independent Accountant was able to independently trace such sales from the Company to Qingdao Beihui and Changsha Best during the period from FY2015 to FY2018 to the Company’s underlying supporting documents, such as sales invoices, packing lists and third-party bills of lading, as well as trace these sales to cash receipts based on the Company’s bank statements. The Independent Accountant also performed a throughput analysis of the “DR’s Secret” SKU³ from the quantity of raw materials purchased by the Company to the quantity of finished goods sold to China for the same period. The Independent Accountant noted that the Company’s sales to the two import agents appear to be valid and supported by sales and delivery documents.</p>

² The Group’s import agents were: (a) 青岛贝汇贸易有限公司 (“Qingdao Beihui”) during the period from January 2012 to September 2015; and (b) 长沙百世特威日用品贸易有限公司 (“Changsha Best”) during the period from September 2015 to June 2018.

³ Throughput analysis was performed only on DR’s Secret SKU as these constitute the majority of sales in China.

	Please refer to paragraph 1.1 of the section entitled “Key Findings of the Independent Review” below and paragraph 9 of the Executive Summary.
To validate the cash received from the sales to the distributors/ customers by the primary import agent.	<p>In respect of the sales of Changsha Best to its customers,⁴ the Independent Accountant was provided with cash movement spreadsheets for FY2017 and FY2018 and was able to trace these movements on a sampling basis to Changsha Best’s bank statements which were obtained independently, but was not able to trace these cash movements to any underlying source documents as these were not available. As an alternative, the Independent Accountant was able to match the sales orders obtained from the distributors of Changsha Best in 2017 and 2018 to Changsha Best’s sales data recorded in the Company’s Customer Relationship Management (“CRM”) System on a sampling basis.⁵</p> <p>In respect of the bank accounts of Changsha Best, the Independent Accountant had relied on the information in these bank statements to categorise the cash movement and have not performed any further work on these cash movements due to the lack of supporting source documents.</p> <p>Please refer to paragraph 1.1 of the section entitled “Key Findings of the Independent Review” below and paragraphs 11 to 16 of the Executive Summary.</p>
Review of cash movement for certain bank accounts from 1 January 2019 up to 31 March 2020.	The Independent Accountant was provided with the bank statements of Vicstar Lifestyle Pte Ltd (“ Vicstar ”) ⁶ , Changsha Best ⁷ and some of the personal bank accounts for the period from 1 January 2019 to 31 March 2020.

⁴ Qingdao Beihui ceased operations in 2015 and was subsequently de-registered on 18 February 2019. As its financial records were not available, the Independent Accountant did not conduct any work on the sales activities of Qingdao Beihui.

⁵ The Company’s CRM System is a sales ordering system through which Changsha Best’s sales to its distributors and customers were processed and tracked.

⁶ By way of background, the Company sold products into China through Vicstar from January 2010 to December 2011, which was prior to the commencement of the Export Model in January 2012. Based on a search conducted with the Accounting and Corporate Regulatory Authority of Singapore on 20 July 2020, Vicstar is still in existence as a private limited company incorporated under the laws of Singapore. Management understands that, as at the date of this announcement, Vicstar is in the process of being struck off.

⁷ While the Independent Accountant was able to independently obtain the bank statements of Changsha Best for the period from 1 January 2019 to 31 December 2019, it was unable to do the same for the period from 1 January 2020 to 31 March 2020 due to travel restrictions, and instead received bank statements for the remaining accounts from Mr. Yan.

	The Independent Accountant's review of the cash movements of Changsha Best and Vicstar is discussed in paragraphs 1.2 and 2.2 of the section entitled "Key Findings of the Independent Review" below.
To identify and make appropriate recommendations on any internal control weakness(es) and breaches of the Singapore listing rules, regulations or local laws as applicable. Where breaches have been identified, to identify the responsible parties if possible.	The Independent Accountant's observations and recommendations on internal control weakness(es) and compliance with the Singapore listing rules, regulations or local laws are set out in paragraph 5 of the section entitled "Key Findings of the Independent Review" below and paragraphs 91 to 96 of the Executive Summary.

Key Findings of the Independent Review

A summary of the key findings of the Independent Review is set out below.

1. Export Model

1.1. Veracity of sales under the Export Model from January 2015 to June 2018

In respect of the Group's sales to import agents⁸ under the Export Model, the Independent Accountant did not note any significant exceptions based on the work performed on the samples selected. The Independent Accountant was able to independently trace such sales from the Company to Qingdao Beihui and Changsha Best during the period from FY2015 to FY2018 to the Company's underlying supporting documents, such as sales invoices, packing lists and third-party bills of lading, as well as trace these sales to cash receipts based on the Company's bank statements. The Independent Accountant also performed a throughput analysis of the "DR's Secret" SKU⁹ from the quantity of raw materials purchased by the Company to the quantity of finished goods sold to China for the same period. The Independent Accountant noted that the Company's sales to the two import agents appear to be valid and supported by sales and delivery documents.

In respect of the sales of Changsha Best to its customers,¹⁰ the Independent Accountant was provided with cash movement spreadsheets for FY2017 and FY2018 and was able to trace these movements on a sampling basis to Changsha Best's bank statements which were obtained independently, but was not able to trace these cash movements to any underlying source documents as these were not available. As an alternative, the Independent Accountant was able to match the sales orders obtained from the distributors of Changsha Best in 2017 and 2018 to Changsha Best's sales data recorded in the Company's CRM System on a sampling basis.

1.2. Cash movement analysis of Changsha Best

⁸ The Group's import agents were: (a) Qingdao Beihui during the period from January 2012 to September 2015; and (b) Changsha Best during the period from September 2015 to June 2018.

⁹ Throughput analysis was performed only on DR's Secret SKU as these constitute the majority of sales to China.

¹⁰ Qingdao Beihui ceased operations in 2015 and was subsequently de-registered on 18 February 2019. As its financial records were not available, the Independent Accountant did not conduct any work on the sales activities of Qingdao Beihui.

The Independent Accountant also attempted to reconcile the total cash receipts and commission payments in Changsha Best's bank statements for FY2017 and FY2018 with the Company's CRM System. In performing the reconciliation exercise, the Independent Accountant found that Changsha Best only recorded approximately 60% of the value of its sales to its distributors / members in its official bank accounts, while proceeds from the remaining 40% of its sales were deposited into six (6) other personal bank accounts not in the name of Changsha Best. From a cash movement analysis, the Independent Accountant found that the monies in the personal bank accounts were subsequently used to make commission payments to distributors / members, sales incentives to employees and transfers to Vicstar.

For the period from 1 January 2017 to 30 June 2018 (end of the Export Model period), the Independent Accountant was able to match payments by Changsha Best to the Company and BW Changsha to the bank statements of the Company and BW Changsha, and the commission payments from the personal bank accounts could be reconciled to the Company's CRM system. However, the Independent Accountant was not able to independently verify the other outflows, such as payments made to Mr. Yan and employees of Changsha Best, to any underlying source documents of Changsha Best as these were not available and most of the payments were made in cash. Based on the official and personal bank accounts used by Changsha Best, these outflows comprised total cash outflows of approximately: (a) CNY56.1 million (equivalent to S\$11.5 million) relating to transfers to Vicstar; (b) CNY40 million (equivalent to S\$8.3 million) relating to sales incentives to Mr. Yan and Changsha Best employees; and (c) CNY335.3 million (equivalent to S\$68.9 million) relating to other operating expenses (*i.e.*, payments for import tax and payments to travel agents) and payments to tax authorities.

For the period from 1 January 2019 to 31 March 2020, the Independent Accountant noted the following based on the information in the bank statements for the official bank accounts of Changsha Best: (a) cash inflows mainly pertain to tax rebates from the tax authorities and the transfer of approximately CNY700,000 from Changsha Best's US\$ account¹¹; (b) commissions mainly pertain to Lifestyle Centre allowances that were subsequently paid out in respect of sales made by the distributors during the Export Model period; and (c) operating expenses mainly pertain to payments to the tax authorities. The Independent Accountant was unable to independently verify the movement as they did not have access to underlying source documents.

1.3. Interactions between the Group and the import agents identified through email reviews

The Independent Accountant has observed that employees of the Group were actively involved with the financial and operational management of the import agents, and employees of the import agents appear to have deferred to Management for various approvals and operational decisions. The Independent Accountant further noted that the Company's employees appear to be in possession of the bank tokens of some of Changsha Best's bank accounts.

¹¹ The US\$ account comprised of Mr. Koh KC's US\$100,000 capital injection in 2017. This account was closed in November 2019 and the amounts transferred to the CNY account of Changsha Best. US\$100,000 translated to approximately CNY700,000.

1.4. Management's Response¹²

Management has represented to the Independent Accountant that save for the shareholder of Qingdao Beihui being Ms. Tan's¹³ ex-neighbour, Mr. Yan being a current employee of BW Changsha, Mr. Koh KC¹⁴, the 监事 (Supervisor) of Qingdao Beihui, being the brother-in-law of Ms. Hoan¹⁵, and the Company's consultant to Qingdao Beihui being the nephew of Ms. Hoan, none of the shareholders or key operational personnel of Qingdao Beihui are employees of the Group, have any direct or indirect relationship with the directors, key management or controlling shareholders of the Group or their associates. While there are significant interactions between the employees of the Group and Changsha Best at the day-to-day operational level, Management has represented to the Independent Accountant that Changsha Best is an independent entity, save for the fact that Mr. Koh KC is the brother-in-law of Ms. Hoan. Beneficial interest in Changsha Best is held by Mr. Yan, Mr. Koh KC and the shareholders of Vicstar.

Management has explained that the Company played a role in the affairs of Changsha Best and Qingdao Beihui to safeguard the interests of the Group and Shareholders. Management implemented control measures, such as requiring final validation for payments made by the import agent and providing product training to the import agents' employees, in order to achieve its principal interests of: (a) safeguarding monies due to the Company for products sold on credit terms; (b) establishing and building its brand equity in the China market; and (c) learning and acquiring market knowledge from the import agent's employees.

As the arrangements concerned the day-to-day operations and sales of the Group's products and only involved an insignificant amount of cash investment by the Group, Management did not involve the AC in discussions pertaining to these detailed operational matters. While the AC was aware of services rendered by the Group to third-party agents, the AC was not aware that the third-party agent was Vicstar, nor was the AC aware that Vicstar and the import agents were strategic partners. They were also not aware of the back-to-back arrangements with Vicstar and the import agents as these operational issues and working arrangements of Vicstar and the import agents were not part of reporting matters to the AC.

¹² Please refer to paragraphs 19 to 26 of the Executive Summary for further details of Management's response on this issue.

¹³ Ms. Doreen Tan ("**Ms. Tan**") is the Company's Co-Founder, Co-Chairman and President.

¹⁴ Please refer to the Company's announcement dated 12 May 2019 for further details of Ms. Hoan's relationship with Mr. Koh KC.

¹⁵ Ms. Dora Hoan ("**Ms. Hoan**") is the Company's Co-Founder, Co-Chairman, Group Chief Executive Officer and Managing Director.

1.5. The Independent Accountant's Recommendations

The Independent Accountant was not able to independently corroborate Management's response set out under paragraph 1.4 above. The Independent Accountant noted that Changsha Best's practice of recording only part of the operations in the "official books" is a concern and has concluded that the extent of the Company's involvement in Changsha Best's operations and financial management exposes it to potential business and regulatory risks in the way the operations have been run and the manner in which Changsha Best's financial records have been maintained. Even though Changsha Best has ceased operations, the Independent Accountant has recommended that the Board should consider seeking legal advice on any potential legal implications to the Group in relation to such practice.¹⁶ The Independent Accountant has further recommended that the Group's external auditors consider the implications, if any, of the above involvement by the Company to the Group's financial statements.

1.6. The Board's Observations

The Board has sought legal advice on the potential legal implications to the Group and, save for the internal controls review discussed in paragraph 5 below, the Board does not envisage any further action to be taken in relation to the matters set out in this paragraph 1, which relate to historical matters that ceased following completion of the Group's transition from the Export Model to the Franchise Model. In particular, the Board has taken note of the following explanations by Management for the arrangements discussed above:

- (a) each of Changsha Best and Qingdao Beihui had separate registered owners and legal representatives independent from Management, the Directors or substantial Shareholders of the Company, save that Mr. Koh KC, the brother-in-law of Ms. Hoan, was the legal representative and sole shareholder of Changsha Best and 监事 (Supervisor) of Qingdao Beihui. However, Mr. Koh KC was only a passive investor in Changsha Best and was not involved in its management or business operations. Mr. Yan was the general manager of Changsha Best and had management control of, and a 80% beneficial ownership in, Changsha Best;
- (b) none of the key operations personnel of Qingdao Beihui and Changsha Best, or the individuals in whose names the identified personal bank accounts were opened, are related to Management, the Directors or the substantial Shareholders of the Company;
- (c) Qingdao Beihui and Changsha Best both had their own employees and were capable of operating independently. Measures granting the Group oversight were intended to safeguard the interests of the Group and Shareholders;
- (d) Management had a justifiable commercial rationale for playing a role in the affairs of Changsha Best and Qingdao Beihui, to ensure that all funds due to the Company were safeguarded and that the Group's brand equity was maintained;
- (e) none of the Management or Ms. Hoan were involved in any profit-sharing agreements between Mr. Koh KC and Mr. Yan, which were negotiated between the two parties independently;

¹⁶ According to a search conducted against Changsha Best on the National Enterprise Credit Information Publicity System at <http://www.gsxt.gov.cn/index.html>, Changsha Best was de-registered on 13 January 2020.

- (f) the Company's arrangements with Changsha Best were governed by the distribution agreement entered into on 1 August 2015, the terms of which were agreed on a willing-seller and willing-buyer basis, after discussions conducted on an arm's length basis on behalf of the Group by Mr. Huang Ban Chin with Mr. Yan. The Company also entered into product rebate agreements dated 1 January 2016 and 1 January 2017 with Changsha Best, pursuant to which Changsha Best was entitled to product rebates for achieving specific purchase targets. The Company's arrangements with Qingdao Beihui were governed by sales distribution agreements dated 1 January 2012 and 1 January 2014; and
- (g) the Group and Shareholders benefitted from the strong demand in China for the Group's products built up by Vicstar and the import agents, which is reflected in the growth in the Group's China revenue from approximately S\$2.6 million in FY2013 to S\$135.8 million¹⁷ in FY2018.

2. Relationship between the Group and Vicstar

2.1. Business activities of Vicstar

Prior to the Export Model, the Company partnered with two top distributors in Singapore to sell products into China through Vicstar, which imported products from the Company from January 2010 to December 2011. Vicstar is owned by the spouses of two top distributors in Singapore. In January 2012, the Company started to sell products to Qingdao Beihui under the Export Model, but Vicstar continued to support the China operations of Qingdao Beihui, and then the China operations of Changsha Best, by maintaining China member database and facilitating the calculation of sales commissions due to the China distributors / members. Based on the contracts between the Company and Vicstar, the Group provided Vicstar with IT services, financial and business management, and personnel support from 2012 in return for a service fee. This included the right for Vicstar to use the Company's CRM system under the Export Model.

The Independent Accountant has observed that Vicstar's audited financial statements were prepared with support from the Group's employees and reflect a back-to-back arrangement whereby Vicstar's purchase and sales figures recorded the purchases by the import agent from the Company, which would then be on-sold by the import agent to Vicstar at a mark-up (*i.e.*, Vicstar's purchases). When the distributors in China purchased the products, the sales orders were keyed into the CRM system and the import agent arranged for the distribution of the products, as well as collection of monies from such sales. The import agent facilitated the payment of commissions to the China distributors and the balance, which represented collections net of commission payments and monies due to the import agents, were transferred by the import agent to Vicstar. A flowchart of this arrangement prepared by the Independent Accountant is set out in paragraph 34 of the Executive Summary. The Independent Accountant has observed that it is unable to establish the commercial rationale of Vicstar's back-to-back arrangement with Changsha Best, and is of the view that the financial statements of Vicstar do not accurately reflect the true commercial substance of its activities.

¹⁷ Please note that this includes approximately S\$4.1 million of manufacturing revenue in China.

2.2. Cash movement analysis of Vicstar

From a cash movement analysis based on Vicstar's bank statements from 1 January 2017 to 31 March 2020, the Independent Accountant noted significant cash inflows of S\$16.8 million over the period, which they were informed were from Changsha Best. The Independent Accountant was unable to trace these inflows to any supporting documents and were informed that the transfers were made through money changers. Based on its reconciliation, using an estimated average exchange rate¹⁸, the Independent Accountant has observed a difference of S\$543,000 between outflows from Changsha Best and inflows to Vicstar. According to Mr. Yan, this difference arose from exchange rate differences, but the Independent Accountant has not been able to confirm this due to a lack of documentary evidence. The Independent Accountant further noted a significant portion of cash outflows from Vicstar, amounting to S\$16.5 million, was eventually paid by Vicstar to the Company as service fees pursuant to the various service agreement signed between Vicstar and the Company, and S\$2.2 million was paid to the two shareholders of Vicstar as dividends and directors' fees. The Independent Accountant has not seen any payments to Mr. Yan for 70% of the net profits of Vicstar / the China operations.¹⁹

2.3. Interactions between the Group and Vicstar identified through email reviews

Vicstar is a separate legal entity from the Group, with its registered owners independent from Management. The Independent Accountant has observed that the Company had assisted in incorporating Vicstar, is substantially involved in its daily operations, such as approval of expenses, and managed the financial affairs of Vicstar, including liaising with external auditors on the financial audit, which the Independent Accountant noted appear to be beyond the capacity of an advisor as defined in the service agreements between the Company and Vicstar. Based on interviews conducted with the shareholders of Vicstar, the Independent Accountant noted that the personnel performing the daily operations and financial activities for Vicstar and assisting to coordinate between the import agents and Vicstar, is an employee of the Company in the Membership Department.

2.4. Management's Response²⁰

Management has represented to the Independent Accountant that Vicstar was initially set up to supply the Group's products in China when the Group was still in the process of obtaining a Direct Selling License. After Qingdao Beihui replaced Vicstar from 2012, Vicstar continued to work with Qingdao Beihui and then with Changsha Best from 2015 as strategic partners, to protect its interests and develop the China market via a pricing arrangement. Since 2012, Vicstar was responsible for managing the use of the CRM system and training arrangements for the import agents and collected fees on behalf of the Group for non-trade transactions, including service fees due to the Group, while the import agents were responsible for the operations, importing and distribution of the Group's products to wholesalers in China. The import agents also supported transactional inputs for the CRM system. This arrangement benefitted the Group as it made it easier for the Group to enforce its legal rights against Vicstar

¹⁸ Published by the Monetary Authority of Singapore.

¹⁹ According to a letter dated 12 June 2020 from the shareholders of Vicstar to the Independent Accountant, Vicstar's arrangement with Changsha Best was that the shareholders of Vicstar had agreed with Mr. Yan that the net profit from the China operations would be split between the shareholders of Vicstar and Mr. Yan under a 30:70 ratio. This agreement was not captured in a formal agreement.

²⁰ Please refer to paragraphs 42 to 49 of the Executive Summary for further details of Management's response on this issue.

which is a Singapore legal entity in the event of any legal disputes concerning the intellectual property rights to the CRM system, and the payment and collection of monies for the maintenance and operation of the CRM system in China. This arrangement of charging service fees to Vicstar, as opposed to Changsha Best and Qingdao Beihui, reduced cross border risk for the Group.

With the commencement of the Franchise Model from July 2018, Vicstar ceased the arrangements with the import agents. Franchisees continued to work with Vicstar till June 2019 to compute commissions as the CRM system previously used by Vicstar and the import agents had sales records which facilitated the computation of commissions payable to the distributors based on the algorithm calculations formatted by the CRM system.

Management has explained that Vicstar had prepared its books based on the business records in the CRM system in order to enable it to monitor the China business transactions, and the Group, through Vicstar's maintenance of parallel customer and financial records (i.e., reflecting a back-to-back arrangement), was able to monitor the China operations of Qingdao Beihui and Changsha Best. Management considers the deployment of the CRM system in China via Vicstar to have been critical for Qingdao Beihui and Changsha Best to develop and support their distribution networks and indirectly the expansion of sales of the Group's products in China. The China market built up by Vicstar and the import agents benefitted the Company in growing the turnover sales of the Group in the China market over the past few years.

As the Company was a supplier and consultant for the import agents and Vicstar, frequent interactions between Vicstar's directors and certain employees of the Company were necessary for the Company to provide services to assist Vicstar and Changsha Best to verify and validate payments. While the Company assisted to coordinate matters concerning the import agents and Vicstar and performed verification of documents on expenses that were incurred in China as Vicstar had no manpower in China, Vicstar's operations in China were supported by the import agent's local manpower resources.

Management has represented to the Independent Accountant that the Group and controlling Shareholders do not have any beneficial interests in Vicstar nor is Vicstar controlled by the Group. All the monies in the bank accounts of Vicstar belong to Vicstar which is wholly-owned by its shareholders and Vicstar's shareholders have confirmed in no uncertain terms that none of such monies are due to or belong to the Company or Management. Management's representation on the above arrangement is supported by a letter dated 12 June 2020 from the shareholders of Vicstar to the Independent Accountant to provide clarification on the business relationship between Vicstar, the import agents and the Group.

2.5. The Independent Accountant's Recommendations

The Independent Accountant was not able to verify that Vicstar's operations in China were supported by the import agent's local man power resources, and was not able to establish the directing mind of Vicstar as they noted the operations of Vicstar appear to be managed by the Company's employees. Accordingly, the Independent Accountant noted the arrangement with Vicstar raises concerns whether such arrangement exposes the Company to legal and regulatory risks given the level of involvement in managing the entity. The Independent Accountant strongly recommended that the Board seek legal advice on the implications, if any, to the Group, and the Group's external auditors consider the implications of the arrangement to the Group's financial statements.

2.6. The Board's Observations

The Board has sought legal advice on the potential legal implications to the Group and, save for the internal controls review discussed in paragraph 5 below, the Board does not envisage any further action to be taken in relation to the matters set out in this paragraph 2, which relate to historical matters that ceased following completion of the Group's transition from the Export Model to the Franchise Model. In particular, the Board has taken note of the following explanations by Management for the arrangements discussed above:

- (a) Vicstar has separate registered owners and directors independent from Management, and the shareholders of Vicstar have confirmed that they were strategic partners with the import agents in the development of the China market for the Group's products;
- (b) the shareholders of Vicstar have confirmed that the monies in Vicstar's bank accounts belong to Vicstar and are not due to or belong to the Company or Management;
- (c) Management had a justifiable commercial rationale for entering into these arrangements with Vicstar in order to better manage cross-border risks. Due to strict restrictions on non-trade payments out of China, the Company charged service fees to Vicstar, as opposed to Changsha Best and Qingdao Beihui, in order to reduce cross border credit risk. Dealing with Vicstar (instead of the China counterparties) also reduced cross-border enforcement risk for the Company for the reasons mentioned above;
- (d) Vicstar's shareholders and their spouses were distributors who spent almost all their time and effort in building sales and customer networks in Singapore and China and had little resources and experience in managing and operating companies. The Company's employees provided assistance per the terms of the service agreement entered into with Vicstar on 1 January 2012, for which the Company received service fees;
- (e) the Group and Shareholders benefitted from the strong demand in China for the Group's products built up by Vicstar and the import agents, which is reflected in the growth in the Group's China revenue from approximately S\$2.6 million in FY2013 to S\$135.8 million²¹ in FY2018; and
- (f) Management has confirmed that the Group no longer has any dealings with Vicstar, which Management understands is in the process of being struck off.

Further, based on the Management's written declarations and the statutory records of Vicstar, the Company did not have any control of the voting power of Vicstar, or any legal right to appoint or remove any director of Vicstar. Consequently, the Board is of the view that Vicstar is not a subsidiary of the Company as defined under the Companies Act (Cap. 50) of Singapore (the "**Companies Act**").

²¹ Please note that this includes approximately S\$4.1 million of manufacturing revenue in China.

3. Franchise Model

3.1. Existence of Franchisees

The Independent Accountant selected eight (8) Franchisees and performed site visits to verify the existence of each Franchisee's physical shop front, which were arranged by BW Changsha. The Independent Accountant also performed four (4) additional surprise visits to other Franchisees. Based on these site visits, interviews conducted with Franchisee owners and Management, the Independent Accountant has made the general observation that the Franchisees' offices do not operate as retail outlets but are used for the conduct of training events or seminars and product demonstrations for potential customers, as well as collection points for members to pick up their purchases.²²

3.2. Veracity of sales from June 2018 to December 2018

In respect of the Company's sales to Best World (China) Pharmaceutical Co., Ltd. (Hunan Branch) (全美世界(中国)药业有限公司湖南分公司) ("BW Changsha")²³ under the Franchise Model, the Independent Accountant did not note any significant exceptions based on the work performed on the samples selected. The Independent Accountant traced the sales and movement of goods from the Company to BW Changsha during the Franchise Model period to third party documents such as bills of lading on a sampling basis, and payments for these goods to the bank statements of the Company and BW Changsha. The Independent Accountant also further performed a throughput analysis of the DR's Secret SKU from the quantity of raw materials purchased by the Company to the quantity of finished goods sold to BW Changsha.

In respect of BW Changsha's sales to significant Franchisees, the Independent Accountant was able to trace such sales recorded in BW Changsha's financials on a sampling basis for the period from 1 June 2018 to 31 December 2018 to underlying invoices, delivery instructions, third party warehouse records and confirmations from third-party logistics providers. As part of its throughput analysis, the Independent Accountant also attempted to reconcile purchases from the Company and sales to Franchisees with BW Changsha's inventory balance as at 31 December 2018. Based on the Independent Accountant's work, the following exceptions were noted:

- (a) potential sales cut-off issue for goods sold which remained undelivered at the third-party warehouse as at 31 December 2018; and
- (b) potential understatement of BW Changsha's sales and certain related expenses.

Goods sold but undelivered at the third-party warehouse as at 31 December 2018

The Independent Accountant observed that there were undelivered goods at the third-party warehouse with an estimated value of approximately CNY111.8 million (equivalent to S\$22.2 million) as at 31 December 2018, which were recorded as sold by the Group in FY2018 as payment for such goods had been received. The Independent Accountant highlighted that this may potentially be a sales cut-off issue for goods sold but undelivered as at 31 December 2018.

²² The Independent Accountant noted from third-party delivery documents that the goods are either delivered to the Franchisees or directly to customers.

²³ BW Changsha, a wholly-owned subsidiary of the Company, operates the Franchise Model in China.

Based on the records of the third-party warehouse, these goods were subsequently delivered in 2019.

Management has performed a subsequent review of all sales to Franchisees and informed the Independent Accountant that the estimated value of sold but undelivered goods as at 31 December 2018 was approximately CNY54 million (equivalent to S\$10.7 million). The Independent Accountant was informed by Management that the differences arose due to the incomplete information in the confirmation provided to the Independent Accountant by the third-party logistics provider, which had omitted deliveries from 25 December 2018 to 31 December 2018. While the Independent Accountant has requested for and received a second confirmation from the third-party logistics provider, they were unable to reconcile the differences through any independent testing.

The Independent Accountant has recommended that the Group's auditors review the computations of Management and consider if any adjustments are required to the sales and inventory numbers for FY2018. Accordingly, relevant adjustments to revenue, cost of sales, distribution costs, trade receivables and trade and other payables were made in the audited financial statements of the Company for FY2018.²⁴

Potential understatement of sales and expenses

The Independent Accountant noted from its testing of BW Changsha's sales to Franchisees that BW Changsha had recognised approximately 80% of the sales value of goods sold to Franchisees based on the tax invoices (*fapiao*) issued, *i.e.*, 80% of the selling price to members. However, members pay 100% of the sales value. In the cash receipts testing performed, the Independent Accountant noted that approximately 20% of the sales value of goods had been deposited into other bank accounts not in the name of BW Changsha.²⁵ The Independent Accountant noted that the outflows from these personal bank accounts include commission payments to members, payments to employees and transfers to Vicstar. From its cash movement analysis of the personal bank accounts from 1 July 2018 to 31 March 2020, the Independent Accountant noted the following:

- (a) approximately CNY397.8 million (equivalent to S\$78.8 million) cash inflows relating to sales and approximately CNY385.1 million (equivalent to S\$76.3 million) cash outflows relating to commission were not recorded in BW Changsha's financial records;
- (b) approximately CNY29.1 million (equivalent to S\$5.8 million) of transfers to Vicstar. Together with approximately CNY56.1 million (equivalent to S\$11.5 million) of transfers to Vicstar from the personal bank accounts during the Export Model period, *i.e.*, 1 January 2017 to 30 June 2018, a total of approximately CNY85.2 million (equivalent to S\$17.3 million) of transfers to Vicstar; and
- (c) approximately CNY63.2 million (equivalent to S\$12.5 million) cash outflows pertaining to payments to employees of BW Changsha, which appear to be sales incentives. Management has informed the Independent Accountant that these payments are in relation to severance payments, bonus payments and payments to Mr. Yan in respect

²⁴ Please refer to Note 2.1 to the Group's audited financial statements for FY2018 contained in the Company's Annual Report for FY2018.

²⁵ The Independent Accountant noted that some of these bank accounts are the same as the accounts mentioned in paragraph 1.2 of the section entitled "Key Findings of the Independent Review" above.

of Changsha Best's operations and that such payouts took place after July 2018. The Independent Accountant has been unable to establish if such payments relate to Changsha Best or BW Changsha as these payments are made to the same individuals who are currently BW Changsha's employees. The Independent Accountant was also unable to independently verify the ultimate recipient(s) of these payments as most payments are made by way of cash.

3.3. Management's Response²⁶

Management's view is that these transactions should not be recorded in the books of BW Changsha, as they were trade rebates given for the benefit of the Franchisees. Accordingly, neither BW Changsha nor the Group had any legal interest in such monies or legal obligations in respect of managing its use. There were no contractual agreements between BW Changsha or the Group and distributors to pay such commissions out of the Franchisees' trade rebates.

The Company had set up BW Changsha with the intention to take over the entire China business from Mr. Yan and his employees. To smoothen the transition, BW Changsha hired the entire Changsha Best sales team set up by Mr. Yan as the team was very experienced and already had an established and successful track record in promoting the Group's products in China. Management was of the view that doing so would ensure minimal disruption to operations on the ground. In addition, the Group would not need to acquire Changsha Best and assume the risks and liabilities associated with the acquisition of a foreign corporate entity.

Mr. Yan was at all times in total control of the payment arrangements and the personal bank accounts. It was the intention that under the Franchise Model, a payment gateway would ultimately be implemented to assist Franchisees with payments of commissions due to their distributors. However, the Franchisees and distributors needed time to work out their respective payment arrangements. Without a limited transition period, it would have been difficult and highly disruptive for Mr. Yan and his team to join BW Changsha. As such, BW Changsha agreed to a one-year transition period starting from 1 July 2018. During the transition period, BW Changsha sold products to the Franchisees at the franchise price, *i.e.*, approximately 80% of the recommended retail price, and the Franchisees on-sold the products to the distributors at the recommended retail prices of the relevant products, giving the Franchisees a margin of approximately 20% as trade rebates. The Franchisees would then pay the commissions directly to the distributors with their 20% margin via the payment arrangements set up by Mr. Yan.

These transitional arrangements ceased on 30 June 2019 with the implementation of a payment gateway to assist Franchisees with payments of commissions due to their distributors. As of the date of this announcement, Franchisees pay 100% of the recommended retail price based on tax invoices (*fapiao*) issued by BW Changsha, and BW Changsha pays marketing fees (which represent the previous trade rebates) and this amounts to approximately 20% of the recommended retail price, *i.e.*, from July 2019, BW Changsha records 100% of the sales to Franchisees as revenue and records these marketing fees as expenses in its books. The Group implemented payment gateway solutions to manage marketing fees payable to the distributors. These payment gateways, which provide payment solutions to individuals / businesses, are service providers licensed by the 中國人民銀行 (People's Bank of China). To the best of Management's knowledge, Mr. Yan's private payment arrangements are no longer in use and Mr. Yan settled all amounts owing to and from Franchisees within a few months after the end

²⁶ Please refer to paragraphs 76 to 84 of the Executive Summary for further details of Management's response on this issue.

of the transition period. The Board will ensure that an internal control and legal review of the payment gateway processes will be included in the review discussed in paragraph 5 below which will be undertaken by an external consulting firm in due course.

As at 31 March 2020, the personal bank accounts only had an aggregate cash balance of approximately S\$3,000.

3.4. The Independent Accountant's Recommendations

The Independent Accountant has not been able to independently verify Management's representations as they noted that the accounts were used not only to pay commission earned by members but also to make various payments to employees, and have not seen evidence to support the position that the monies belong to the Franchisees. The Independent Accountant has highlighted that, in its view, from a financial perspective, all cash movements relating to BW Changsha should be fully and accurately recorded in BW Changsha's books, *i.e.*, total sales revenue and any corresponding trade rebates, commission expenses or incentive payments to employees should be fully recorded as BW Changsha's income and expenses. The Independent Accountant has recommended that:

- (a) Management obtain legal advice on whether the manner in which these transactions have been recorded in the Group and BW Changsha were in compliance with section 199 of the Companies Act;
- (b) the Board work with the Group's auditors to review and consider if any reclassification or adjustments are necessary to the financial statements for FY2018 and FY2019 to ensure the Company's records represent a complete and accurate view of its financial affairs; and
- (c) the Board seeks a formal legal opinion on the legal and regulatory implications of the potential understatement and the above arrangement.

In the event the sales and expenses of BW Changsha have not been fully recorded, the Independent Accountant noted that this may constitute a breach of:

- (i) Section 199(1) and 199(2A) of the Companies Act which requires companies incorporated in Singapore to keep accounting and other records to sufficiently explain the transactions and financial position of the company and to maintain an adequate system of internal accounting controls to provide reasonable assurance that assets are safeguarded and transactions recorded;
- (ii) Rule 703 of the SGX Listing Rules which requires companies to announce information that may affect the price or value of its securities; and
- (iii) Rule 719(1) of the SGX Listing Rules which requires companies to have adequate and effective internal controls and risk management system.

The Independent Accountant has further recommended that the Board seeks legal advice on the implications of the above potential breaches and thereafter take the necessary remedial action.

3.5. The Board's Observations

The Board has noted the findings of the Independent Accountant, as well as Management's representations in relation to the matter, in particular:

- (a) the Group had implemented an accounting system for its China operations under the Franchise Model, through which all sales transactions and volumes of BW Changsha were recorded and duly reflected in BW Changsha's accounts. The Company at all times had full access to and control over the accounting system, which the Company relied on in order to prepare its financial statements; and
- (b) the trade rebates were not booked as revenue, and the commissions and other payments made out of the trade rebates were not recorded as expenses, as Management was of the view that BW Changsha did not have any legal interest or rights in the monies comprising the trade rebates. From July 2019, BW Changsha now has full legal interest and rights in these monies (which represent the previous trade rebates) and fully records these as revenue and marketing fees.

The Group had prepared its financial statements on the basis that BW Changsha was not legally entitled to the trade rebates, which should be attributed to the Franchisees under the oral agreements made between Mr. Yan, in his capacity as General Manager of Changsha Best, and the Franchisees during the transitional period. As mentioned in paragraph 3.3 above, the Franchisees now pay 100% of the recommended retail price, which is fully recorded as BW Changsha's revenue, and BW Changsha pays marketing fees (which represent the previous trade rebates) which amounts to approximately 20% of the recommended retail price, which is fully recorded as BW Changsha's expenses.

The Board has received advice from M&T that oral contracts are valid and enforceable under the laws of China. Further, M&T has reviewed a counter authorization letter signed between BW Changsha and a Franchisee on 1 January 2020 ("**Counter Authorization Letter**")²⁷. Although the term of the Counter Authorization Letter does not cover the Franchise Model period from 1 June 2018 to 31 December 2019, M&T has stated that the Counter Authorization Letter may constitute indirect evidence to support the oral agreements between Mr. Yan and the Franchisees. As at the date of this announcement, neither Mr. Yan nor any Franchisee has disputed the oral agreements, and have in fact duly performed their respective obligations under the oral agreements. Based on Management's representation to M&T, the personal bank accounts were used to pay commissions earned by members and employee's severance and bonus payments, as well as payments to Mr. Yan in respect of his share of profits from Changsha Best's operations. As M&T has observed that Changsha Best and BW Changsha shared the use of some of the personal bank accounts and the former employees of Changsha Best are now employees of BW Changsha, M&T has noted that it is unable to determine if payments made from these accounts relate to Changsha Best or BW Changsha and consequently, unable to determine who the accounts belong to.

M&T has advised that in the event that BW Changsha is determined to be the owner of the trade rebates and the trade rebates were not recorded as income in BW Changsha's financial

²⁷ According to the Counter Authorization Letter, BW Changsha is authorised to pay sales commission (销售佣金), labor remuneration (劳务报酬), labor fees (劳务费), and consulting service fees (咨询服务费) to, and withhold personal income tax (个人所得税) from, the Franchisee's sales staff on behalf of the Franchisees.

statements, BW Changsha could be subject to administrative punishments which include, amongst others, an order to make corrections to the accounts, to pay a fine of between CNY3,000 and CNY100,000 (inclusive) and/or to pay the unpaid or underpaid taxes and late payment fines, and concurrently receive a fine of between 50% of and five times the amount of taxes unpaid or underpaid (inclusive).

The Board has also obtained legal advice on section 199 of the Companies Act and is of the view that the provision does not apply to foreign subsidiaries. Section 199(1) does not expressly require a Singapore-incorporated company to keep the underlying records which are the property of its foreign-subsiaries. Section 199(2A) imposes an obligation on a Singapore public company and each of its Singapore-incorporated subsidiaries to devise and maintain a system of internal accounting controls sufficient to provide a reasonable assurance that, amongst others, transactions are properly authorised and recorded as necessary to permit the preparation of true and fair financial statements.

Notwithstanding the above, the Board will consult the Company's external auditors and engage an independent accounting adviser to review and ascertain the appropriate accounting treatment of the trade rebates and will update Shareholders in due course.

4. Legality of the Franchise Model

4.1. The Independent Accountant's Recommendations

The Independent Accountant noted that with the Group's transition to the Franchise Model, the manner in which sales were conducted through the member network and the basis of computation of commission remained unchanged from the Export Model. The Independent Accountant has identified seven (7) distributor / member ranks under the Export Model, and observed that the Group mapped these existing distributor / member ranks into four (4) tiers under the Franchise Model, Franchisee, Area Representative²⁸, Sales Representative and VIP. Under the Franchise Model, the Group selected 28 distributors from the Export Model and entered into franchise agreements with them, as well as Area Representatives and Sales Representatives, on a non-mutually exclusive basis.²⁹ Management has informed the Independent Accountant that the Franchise Model as currently structured is in compliance with local China regulations and the Franchise License.

The Notice of Compliance required the Company to obtain the Legal Opinion. The Independent Accountant also recommended that the Board obtain the advice of an independent and suitably qualified Chinese law expert to comment on the legality of the structure of the Group's sales and distribution business under the Franchise Model under local China regulations and whether it falls within the scope of the Franchise License. Accordingly, the Company engaged M&T, an independent law firm in China, to provide the Legal Opinion on the legality of the Group's sales and distribution model under the Franchise Model. Based on the information of the business model under the Franchise Model (including the sales and distribution process) provided by the Company and M&T's review of the description of the business model in the Report, M&T has advised that BW Changsha is qualified to engage in franchise business in China and has completed relevant record filings for franchise as required from 1 June 2018 to 31 December 2019, and the business model complies with franchise related laws and regulations in China.

²⁸ An Area Representative may be a Province Representative or City Representative.

²⁹ Should a distributor be eligible, that distributor may enter into all three (3) types of contracts with BW Changsha. BW Changsha does not enter into any contracts with VIPs as there are no commissions due to VIPs.

However, M&T has highlighted that certain features of the Franchise Model may pose potential risks under other laws in China.

Shareholders should also note that the Company had previously obtained an opinion from Beijing Dacheng Law Offices, LLP (part of the global law firm Dentons), one of the largest law firms in China, that, following review of the information provided, the payments made under the Franchise Model (Franchisee Fee, Consulting Service Fee and Labour Fee) are in compliance with applicable laws and regulations.³⁰

4.2. The Board's Observations

The Board has considered the advice provided by M&T, which noted that the Franchise Model is in compliance with applicable franchise related laws and regulations in China, but that certain features of the Franchise Model may pose potential risks under other laws in China.

Firstly, M&T noted that there remains some ambiguity in whether the Sales Representatives, Province Representatives and City Representatives (collectively, "**Representatives**") promote products on behalf of BW Changsha or the Franchisees, despite reviewing the Counter Authorization Letter dated 1 January 2020 which may constitute indirect evidence that such representatives promote products on behalf of the Franchisees. In the event that the relevant authorities disagree with the Group's position and find the Representatives to be sales representatives of BW Changsha (as opposed to the Franchisees), and that the Representatives sold relevant products to ultimate consumers outside of BW Changsha's fixed places of business, they may find BW Changsha guilty of conducting direct selling³¹ without a licence. If such a finding were to be made, BW Changsha may be subject to administrative punishments which include confiscation of its direct selling products and illegal sales income, as well as a fine of between CNY50,000 and CNY500,000 (inclusive), and may be banned from operating. Further, the business license of the branch of a direct selling company which has illegal operations may be revoked. Where a direct selling company no longer satisfies the conditions under its direct selling license, its license may be revoked.

Secondly, BW Changsha paid Consulting Service Fees and Marketing/Promotion Fees to Province Representatives and City Representatives based on the individual member's purchases and the purchase volume of that member's group.³² M&T has observed that as members of the "members group" are directly or indirectly recruited by the Province Representatives or City Representatives, and Province Representatives and City Representatives receive commissions based on the purchase volume of that "member's group", such a commission structure may constitute one of the situations indicative of a ChuanXiao scheme in violation of ChuanXiao³³ related provisions under China law. In the event that the commission structure is determined to contravene ChuanXiao related provisions, BW Changsha may be subject to administrative punishments that include the confiscation of illegal

³⁰ Please refer to the Company's announcements made on 23 February 2019 and 9 May 2019.

³¹ Under the direct selling laws in China, two conditions must be met at the same time to constitute direct selling: (a) selling directly to ultimate customers; and (b) such sales occurs outside the fixed place of business.

³² Province Representatives and City Representatives are considered upper-level representatives while the members of the "members group" which are sales representatives are considered lower-level representatives.

³³ The term "ChuanXiao" refers to such an act whereby an organizer or operator seeks for unlawful interests to disturb the economic order and affect the social stability by recruiting persons, calculating and paying remunerations to recruiters on the basis of the number of persons a recruiter has directly or indirectly recruited or the sales performance of the persons recruited, or asking the recruiters to pay a certain fee for obtaining the qualification for participation.

properties and gains, a fine of between CNY100,000 and CNY2,000,000 (inclusive), and/or suspension of operations for rectification or revocation of its business license. As BW Changsha has confirmed that the sole objective of its business activities was the sale of products in China and its business does not profit from recruiting persons and remunerating recruiters on the basis of the number of persons recruited, or requiring recruiters to pay to participate, M&T opined that BW Changsha is unlikely to be subject to criminal liability³⁴ and may only receive administrative punishments (if found guilty of contravening ChuanXiao related provisions). M&T further highlighted that it has observed that, in practice, the competent authority is usually very cautious in determining ChuanXiao behavior.

As stated above, the Group has decided to transition from the current Franchise Model to direct selling in China, and is currently formulating its strategy for the eventual transition. The Board believes that any issues which have been observed by M&T in relation to the Franchise Model should be resolved once the Group has transitioned to direct selling in China. In the event any of the risks observed by M&T materialises, the Board will work with its legal advisers to mitigate against any potential administrative penalties or disruption to the Group's sales in China.

5. Compliance with the Code of Corporate Governance

The AC has taken note of the Independent Accountant's closing observations that the Group may be required to explain if they have deviated from Principles 6, 10 and 11 of the 2012 Code of Corporate Governance, and Provision 1.6 and Principle 9 of the 2018 Code of Corporate Governance. The Board has also taken note of the Independent Accountant's recommendation that the AC undertakes the following immediately:

- (a) a comprehensive risk assessment to identify all potential legal, financial and business risks faced by the Group, and formulation of an action plan on such risks identified;
- (b) a thorough review of the Group's corporate governance, legal and compliance processes and to put in place formal policies moving forward. The AC should consider appointing a senior compliance officer reporting directly to the AC to implement any agreed remedial actions and to take all necessary steps to oversee the compliance function; and
- (c) a thorough review of the overall corporate structure of the Group to identify if similar structures exist in the Group and ensure that these are in compliance with local and Singapore regulations.

In view of the matters arising out of the Report, the Board plans to engage an external consulting firm to work with its legal advisers to consider the recommendations of the Independent

³⁴ "Network Remuneration" is a type of ChuanXiao activity whereby an organiser or operator seeks for unlawful interests to recruit persons to participate in a ChuanXiao scheme and asks recruiters to persuade others to participate in the scheme so as to form a multi-level relationship, and calculates and pays remuneration to an upper-level promoter on the basis of the sales performance of the promoters below. Where an organisation takes the form of "Network Remuneration", but the real purpose of its business operations is to sell commodities, such activities will not be treated as a criminal offence and such an organisation may only receive administrative punishments (if found guilty of contravening ChuanXiao related provisions).

The criminal liability for violation of ChuanXiao related provisions under China law is that if more than 30 people are involved in ChuanXiao activities within an organisation and the level is above three levels, the organiser and leader shall be sentenced to fixed-term imprisonment not more than five years or criminal detention, and be fined; or if the circumstances are serious, shall be sentenced to fixed-term imprisonment not less than five years, and be fined.

Accountant and undertake a diagnostic review of the Group's existing corporate governance, legal and compliance processes, as well as the accounting practices highlighted as an area of concern in the Report. In addition, the Board, in due course, will appoint a senior compliance officer to implement any agreed remedial actions and to take all necessary steps to oversee the compliance function, who will report directly to the AC.

Further action

The Board will update Shareholders on the steps taken and to be taken in due course. The Board will continue to take all necessary actions to safeguard the interests of Shareholders and the Group.

Shareholders are reminded that the trading suspension of the Company's shares will continue following this announcement and will only be lifted after the Company has submitted a trading resumption proposal pursuant to Rule 1304 of the Listing Manual and upon fulfilment of the conditions required by SGX RegCo, including the finalisation of the Group's audited financial statements for FY2019, and SGX RegCo indicating that it has no objections to the resumption proposal.³⁵ The Board will make further announcement(s) as and when there are any material developments on this matter.

BY ORDER OF THE BOARD

Huang Ban Chin
Director and Chief Operating Officer
23 July 2020

³⁵ Please refer to the announcement made by SGX RegCo on 9 May 2019 in relation to the trading suspension of the Company's shares.

Annex
Executive Summary

***Best World
International
Limited***

23 July 2020



Executive Summary

Background and appointment of PwC as Independent Accountant

1. Pursuant to a news article published in the Business Times on Best World International Limited (“BWI” or together with its subsidiaries, the “Group”) which raised certain concerns over the Group’s sales transactions under the new Franchise Model, PricewaterhouseCoopers Advisory Services Pte. Ltd. (“PwC” or “we”) was appointed on 18 March 2019¹ to perform an independent review on the financial affairs of 全美世界（中国）药业有限公司湖南分公司 (“BW Changsha”) focusing on the following key areas:
 - (a) To verify the existence of the Franchisees as at 31 December 2018;
 - (b) To validate the sales to the significant Franchisees (by sales value);
 - (c) To validate the cash received from the sales to the significant Franchisees; and
 - (d) To identify and make appropriate recommendations on any internal control weakness(es) and breaches of the Singapore listing rules, regulations or local laws as applicable. Where breaches have been identified, to identify the responsible parties if possible.
2. As a result of the circumstances surrounding the previously undisclosed relationship with the primary import agent in China, and pursuant to the issuance of the Notice of Compliance (the “Notice”) by Singapore Exchange Regulation Pte Ltd (“SGX RegCo”) on 13 May 2019, PwC was directed to perform the following additional work and to report solely to SGX RegCo on the findings pursuant to the independent review:
 - (a) To establish the facts and circumstances surrounding the establishment, appointment and business relationship with the primary import agent;
 - (b) To verify the sales to the primary import agent and other import agents used by the Group in the China market, if any, for the period from FY2015 to FY2018 under the Export Model², and ascertain if these transactions were on normal commercial terms and conducted at an arm’s length basis; and
 - (c) To validate the cash received from the sales to the distributors/ customers by the primary import agent.
3. In addition, SGX RegCo had further instructed PwC to extend the review of cash movement for certain bank accounts from 1 January 2019 up to 31 March 2020.
4. On 22 March 2020, PwC issued an interim update on the independent review based on the work performed up to that date subject to certain outstanding work that was still in progress. We have now completed our work to the extent reasonably practicable based on documents/ information that has been made available to us.

¹ Announcement by the Group made on 19 March 2019.

² The model adopted by the Group prior to 1 July 2018 for its operations in China in which BWI sold to import agents in China.

5. This report sets out all our findings to date and incorporates those highlighted in the interim update as well.

Overview of the Group's China operations

6. We understand from BWI Management³ that in the early years, China customers frequently purchased products from Singapore outlets. Recognising the potential demand for the Group's products, BWI Management completed the set-up of a manufacturing facility in Shanghai in 1996 in order to tap into the domestic China market. However, the Group's China strategy was disrupted by the Asian Financial Crisis in July 1997 and the ban on Direct Selling ("DS") and Multi-level Marketing activities in China in April 1998. With China's accession to the World Trade Organisation ("WTO") in 2004, China authorities liberated the Direct Selling industry in 2006 with the issuance of its first Direct Selling License ("DSL"). While this opened the opportunity for the Group to re-enter the market through joint ventures with local licensed partners, their attempts were unsuccessful.
7. To continue selling into the China market, BWI partnered with two of its top distributors in Singapore (please see (a) below). Over time as the business grew, new entities were incorporated in China as import agents. BWI would sell products directly to these import agents who will then on-sell into the market ("Export Model"). In 2018 when the Group was able to obtain its Franchise License, it ceased operating through the import agents and transitioned the business into the Franchise Model operating under its subsidiary, BW Changsha. The various entities which were involved (see below for details) in the China operations during the period leading to the Franchise Model were:
 - (a) Vicstar Lifestyle Pte Ltd ("Vicstar") – January 2010 to December 2011. This company is owned by two individual shareholders who are the spouses of two Singapore distributors. BWI sold directly to Vicstar from early 2010 but this ceased in December 2011. We were informed that Vicstar continued to work with the import agents to develop the China market during the Export Model period. In particular, Vicstar maintained the China member database, facilitated the calculation of commissions due to distributors, and helped organise trainings and events for China distributors. According to the shareholders of Vicstar, under the arrangement with Changsha Best (please see (c) below), the net profit from the China operations is to be split between the shareholders of Vicstar and Mr. Yan Weijun ("Mr. Yan") under a 30:70 ratio respectively. We were informed that Mr. Yan, a Chinese citizen, was the general manager of Changsha Best and was responsible for the management and business operations of Changsha Best.

³ The Executive Directors of BWI together with the Group Financial Controller of BWI.

- (b) 青岛贝汇贸易有限公司 (“Qingdao Beihui”) – January 2012 to September 2015. This company is owned by one individual shareholder who is also the legal representative of the company. Ms. Doreen Tan (“Ms. Tan”) informed us that the shareholder was an ex-neighbour of hers. We were further informed by BWI Management that this was a nominee shareholder and Qingdao Beihui was beneficially owned by the key operations personnel of Qingdao Beihui who was responsible for the management and business operations. From our corporate search of Qingdao Beihui, we note that Mr. Koh Kim Chuan (“Mr. Koh KC”) (please see (c) below) was registered as the 监事 (Supervisor). We were informed that while Mr. Koh KC was named as the 监事 (Supervisor), he was merely a nominee. Qingdao Beihui was set-up as an import agent as the China market grew and demand for BWI products increased. This was the first import agent in China. We were informed that Qingdao Beihui ceased business in 2015 due to the poor health of the key operations personnel, who has since passed on.
- (c) 长沙百世特威日用品贸易有限公司 (“Changsha Best”) – September 2015 to June 2018. Changsha Best took over the role as the import agent from Qingdao Beihui in 2015. This company is owned by Mr. Koh KC who is the brother-in-law of Ms. Dora Hoan (“Ms. Hoan”). Mr. Koh KC is also the legal representative of the company. We were informed that Mr. Koh KC had invested USD100,000 (equivalent to SGD139,000) into Changsha Best but was only a passive investor. We were further informed that Mr. Yan was the main beneficial owner of Changsha Best. Based on an agreement between Mr. Koh KC and Mr. Yan dated 2 April 2014, Mr. Koh KC is entitled to 20% of the net profits of Changsha Best⁴.

Export Model

8. As our scope of work covered the period from FY2015 to FY2018, we initially focused our review on the two import agents, Qingdao Beihui and Changsha Best. However, in performing our work we note that Vicstar continued to be closely involved in the operations of the import agents and paid significant service fees to BWI during the relevant period. We therefore included this entity in our review. Our findings on these three entities are summarised below.

⁴ The agreement was for a period of five years starting from 30 April 2014 to 30 April 2019. Upon expiry of the agreement, Mr. Yan will distribute 20% of the net profits of the company to Mr. Koh KC.

Business activities of the import agents

BWI's sales to Qingdao Beihui and Changsha Best

9. In respect of BWI's sales to the import agents, we did not note any significant exceptions based on the work performed on the samples selected. We were able to independently trace such sales from BWI to Qingdao Beihui and Changsha Best during the period from FY2015 to FY2018 to BWI's underlying supporting documents i.e. invoices, packing lists and third-party bill of lading. We were also able to trace these sales to cash receipts based on BWI's bank statements. Further, we also performed a throughput analysis of the "DR's Secret" Stock Keeping Unit ("SKU")⁵ from the quantity of raw materials purchased by BWI to the quantity of finished goods sold to China for the same period. From our review, BWI's sales to the two import agents appear to be valid and supported by sales and delivery documents.
10. We were informed that Qingdao Beihui ceased operations in 2015 and was subsequently de-registered on 18 February 2019. We were also told that the documents were not kept as the key operations personnel had passed away. As Qingdao Beihui's financial records were not available, we were not able to perform any further work on the activities of Qingdao Beihui.
11. With regard to Changsha Best, we were informed that records prior to FY2017 were not available as the company had moved to a smaller premise and these records were not kept. For FY2017 and FY2018, we were provided with cash movement spreadsheets and were able to trace these movements on a sampling basis to Changsha Best's bank statements which we obtained independently. However, we were not able to trace these cash movements to any underlying source documents⁶ as these were not available.
12. As an alternative, we requested for Changsha Best's sales data recorded on the Customer Relationship Management ("CRM") system⁷. On a sampling basis, we obtained the sales orders from the distributors of Changsha Best spanning across 2017 and 2018. We were able to match these sales orders to the CRM system.

Cash movement analysis of Changsha Best

13. We attempted to reconcile the total cash receipts and commission payments in the bank statements of Changsha Best for FY2017 and FY2018 to BWI's CRM system. Through our reconciliation exercise we found that Changsha Best only recorded approximately 60% of the value of its sales to distributors/ members in its official bank accounts. Proceeds from the remaining 40% of its sales had been deposited into six other personal bank accounts. Three of these bank accounts were in the name of the spouse of a BWI employee. We were informed by Mr. Yan that he had sought help from these individuals to open the accounts on his behalf.

⁵ Throughput analysis is performed only on "DR's Secret" SKU as these constitute the majority of sales to China.

⁶ Underlying source documents such as third-party documents supporting inflow of funds from individual distributors/ members to sales orders, third-party delivery documents, payment vouchers supported by vendor/ distributor invoices evidencing nature of payments etc.

⁷ BWI's CRM system is used as a sales ordering system, which tracks all product sales made to distributors/ members and computes the commission earned and payable to these distributors/ members based on the sales orders. We understand that Changsha Best's sales to its distributors/ members are also processed and tracked through this system.

14. From our cash movement analysis, it would appear that monies in the personal bank accounts were used to receive sales proceeds and subsequently used to make commission payments to distributors/ members and sales incentives to employees⁸. We also noted cash outflows which Mr. Yan informed were monies transferred to Vicstar.
15. For the period from 1 January 2017 to 30 June 2018 (end of Export Model period), apart from the payments to BWI and BW Changsha which we were able to match to the bank statements of BWI and BW Changsha, and the commission payments from the personal bank accounts which we were able to reconcile to BWI's CRM system, we were not able to independently verify the other outflows to any underlying source documents of Changsha Best as these were not available. We were also not able to independently verify the payments made to Mr. Yan and Changsha Best employees as most of these were made in cash. Based on the official and personal bank accounts used by Changsha Best, these outflows are as follows:
 - (a) Total cash outflows of approximately CNY56.1 million (equivalent to SGD11.5 million) relating to transfers to Vicstar;
 - (b) Total cash outflows of approximately CNY40 million (equivalent to SGD8.3 million) pertaining to sales incentives to Mr. Yan and Changsha Best employees; and
 - (c) Total cash outflows of approximately CNY335.3 million (equivalent to SGD68.9 million) relating to other operating expenses (i.e. payments for import tax and payments to travel agents) and payments to tax authorities.
16. As at 31 March 2020, the bank balances in the official and personal bank accounts are CNY1,000 (equivalent to SGD200) and CNY15,000 (equivalent to SGD3,000) respectively⁹. While we have not seen any direct return of funds or capital to Mr. Koh KC from the official and personal bank accounts for his investment, we were shown a bank statement in the name of Mr. Koh KC indicating total receipts of SGD138,000 (USD100,000) that was received in March 2020. We were informed by BWI Management that these monies were Mr. Koh KC's capital contribution in Changsha Best.

Interactions between the Group and the import agents identified through email reviews

17. From our email reviews, we see BWI employees assisting and supporting the operations and activities of the import agents. In some instances, BWI employees also approve various operating expenses to be incurred by Qingdao Beihui and Changsha Best, and also appear to be in possession of the bank tokens of some of Changsha Best's bank accounts. We also note from our interviews that none of the shareholders of these two entities are involved in the operations in China.
18. It is unclear what is the nature of the relationship between these entities and BWI. BWI Management represented that none of these entities are related to the Group.

⁸ We were given direct access to five of the six personal bank accounts via bank tokens. For the remaining bank account, we were informed that the bank account was frozen and could not be accessed via online.

⁹ Please see Franchise Model section for details on the cash movement for the period 1 July 2018 to 31 March 2020.

BWI Management's response

19. *BWI had intended to expand in China through a DS model, and to acquire a DSL in order to do so. However, given that more time would be required to obtain a DSL, the Group decided to start its entry into China through the Export Model to penetrate the China market and build up brand recognition for its products as soon as possible. Two distributors in Singapore who were previously involved in the selling of the Group's products in China approached the Company and expressed their intention to continue exporting the Group's products to China through Vicstar that was set up in Singapore by their spouses. Vicstar was the first import agent of the Group that marked the start of our Export Model and the assignment of the Group's business in China to a third-party agent was disclosed in the Company's announcement for 4Q2009 results. This arrangement was intended to be temporary.*
20. *To effectively manage the customers database, BWI designed a CRM system for Vicstar, which recorded their transactions for China market. In 2012, one of the distributors in China, applied to become an agent to directly import our products into China. However, Vicstar's shareholders and their spouses were concerned that the China agent may use their own CRM systems that could result in Vicstar losing the entire database and may even lose all their distributors in the worst-case scenario. Vicstar eventually decided to work together with the import agents as strategic partners to develop the China market together.*
21. *Qingdao Beihui was set-up as a wholly foreign-owned entity ("WFOE") to achieve better market credibility as an importer of foreign brands and enjoyed certain advantages in applying for certain relevant permits and licenses. Save for the shareholder of Qingdao Beihui being Ms. Tan's ex-neighbour, Mr. Yan being a current employee of BW Changsha, Mr. Koh KC as the 监事 (Supervisor) of Qingdao Beihui being the brother-in-law of Ms. Hoan, and the BWI consultant to Qingdao Beihui being the nephew of Ms. Hoan, none of the shareholders or key operational personnel of Qingdao Beihui are employees of the Group, have any direct or indirect relationship with the directors, key management or controlling shareholders of the Group, or an associate of such director, key management or controlling shareholders. During 2015, the distributor (i.e. the key operations personnel of Qingdao Beihui) expressed his intention to discontinue the business due to ill health. Mr. Yan, who was the marketing manager of Qingdao Beihui at that time, took over the operations.*
22. *Mr. Yan then approached Mr. Koh KC (who is the brother-in-law of Ms. Hoan) to be a passive investor, while Mr. Yan would be responsible for all operational matters. Changsha Best was set up by Mr. Yan as a WFOE, to take over the role as the Group's China import agent from Qingdao Beihui. As Mr. Yan had for all intents and purposes management control of Changsha Best, BWI only dealt with Mr. Yan. Neither BWI Management nor Ms. Hoan were involved in any profit-sharing agreements between Mr. Koh KC and Mr. Yan, which were negotiated between the two parties independently.*

23. *Mr. Yan and his employees were aware that they would eventually join the Group and would assist BWI to prepare to take over the China distribution. With this common understanding, Changsha Best and BWI employees worked very closely with the common objective to ensure that day to day operations would not be disrupted during the takeover. In many instances, as Changsha Best had the relevant local experience and resources, Changsha Best employees will also offer assistance in the areas of administrative matters of the Group's companies, such as routine administrative matters relating to dormant China subsidiaries, and selection of location and design and renovation of the new BW Changsha office. The Group did not see the need to engage a separate set of full-time employees to handle such matters at that time.*
24. *While there are significant interactions between Changsha Best employees and BWI employees at the day to day operational level, Changsha Best is an independent entity, save for the fact that Mr. Koh KC is the brother-in-law of Ms. Hoan. Beneficial interest in this entity is held by Mr. Yan, Mr. Koh KC and the shareholders of Vicstar.*
25. *In working with Vicstar and the import agents, BWI had three principal interests: (1) to ensure the collection of monies due to BWI for the products sold on credit terms; (2) to establish and build its brand equity in the new market; and (3) to learn and acquire market knowledge. In order to achieve the foregoing objective, BWI implemented various measures, such as:*
 - (a) *Controlling the final validation for payments made by the import agents to ensure that monies were not dissipated or utilised before settlement of amounts due to BWI;*
 - (b) *Providing product training to the import agents' employees to ensure that the Group's products are marketed and promoted in a manner consistent with the Group's established brand values; and*
 - (c) *Monitoring the expenditure specifically for product registration, complainant settlement cases, public relations and its related discretionary expenses.*
26. *The above measures were put in place by BWI Management to secure the interests of the Group. The objective was to ensure that all funds due to BWI were safeguarded and that the Group's brand equity was maintained. The arrangements concerned the day to day operations and sales of the Group's products. In addition, as the arrangements involved only an insignificant amount of cash investment by the Group, BWI Management did not involve the Audit Committee of BWI (the "AC") in any discussion pertaining to such detailed operational matters. While the AC was aware of services rendered by the Group to third-party agents, the AC was not aware that the third-party agent was Vicstar, nor was the AC aware that Vicstar and the import agents were strategic partners. They were also not aware of the back-to-back arrangements with Vicstar and the import agents as these operational issues and working arrangements of Vicstar and the import agents were not part of reporting matters to the AC.*

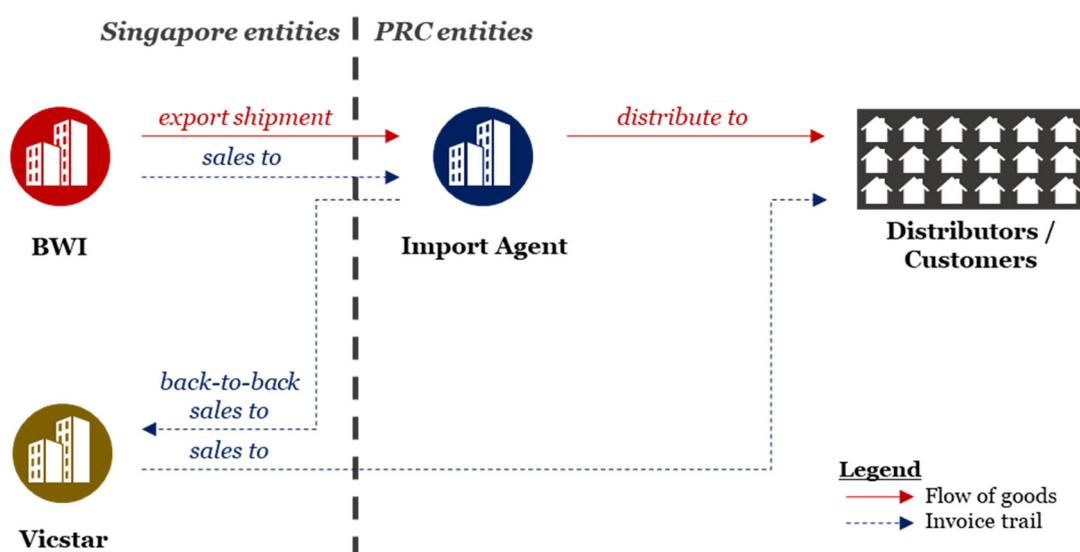
PwC's Observation

27. We are not able to independently corroborate BWI Management's response. From our email review, we note that BWI was very much involved with the financial and operational management of the import agents. Import agents' employees appear to be deferring to BWI Management for various approvals and operational decisions.
28. We have not seen any active involvement by the shareholders of Qingdao Beihui and Changsha Best. In our interview with Mr. Koh KC, he claimed that he was not aware that he was the sole shareholder nor was he aware that he held 100% shares in Changsha Best. We had requested for an interview with the shareholder of Qingdao Beihui, but was informed that the shareholder was unwell and not able to meet.
29. When interviewed, Mr. Koh KC also claimed he was not aware of the performance of the company (i.e. Changsha Best) and only stated that he is entitled to a 20% share of the profits, if any. When asked why he injected his funds only in 2017 instead of in 2014 when he supposedly signed the agreement with Mr. Yan, he stated that Mr. Yan had not requested for the funds then. When asked why he was entitled to 20% of the net profit even though he was a 100% shareholder, he stated that this was the agreed profit-sharing percentage for being a passive investor and for investing USD100,000 (equivalent to SGD139,000) despite him being the 100% shareholder. We are unable to understand the underlying commercial rationale for the arrangement. We have also not seen any documents to evidence Mr. Koh KC's receipt of his 20% share of net profit.
30. Changsha Best's practice of recording only part of the operations in the "official books" is a concern. While we note BWI Management's responses, the extent of BWI's involvement in the Changsha Best's operations and financial management exposes it to potential business and regulatory risks in the way the operations have been run and the manner in which the financial records of Changsha Best have been maintained. Even though Changsha Best has ceased operations, the Board of Directors of BWI (the "Board") should consider seeking legal advice on any potential legal implications to the Group in relation to such practice. We further recommend that the Group's external auditors consider the implications, if any, of the above involvement by BWI to the Group's financial statements.

Business activities of Vicstar

31. Based on the contracts between BWI and Vicstar, the Group provided Vicstar with information technology ("IT") services, financial and business management, and personnel support from 2012 in return for a service fee.
32. We were informed by BWI Management that Vicstar was given the right to use BWI's CRM system. Through this system, Vicstar supported the China operations of Qingdao Beihui and Changsha Best by maintaining the China member database and facilitating the calculation of commissions due to the China distributors/ members. Vicstar also helped develop the China market by organising trainings and events for the China distributors.

33. However, from our interviews with the shareholders of Vicstar, they stated that they do not perform any operational function except to authorise payments as signatories. We note that Vicstar does not have any employees and its affairs had been managed by BWI employees. We were informed that Vicstar also shares the import agent's local manpower resources.
34. From our interviews with BWI Management and our review of BWI's sales to the import agents, we note that BWI ceased selling to Vicstar and sold directly to the import agents after 2011. However, it appears from Vicstar's audited financial statements prepared with support from BWI employees that all purchases by the import agent from BWI and all sales by the import agent to the distributors in China continue to be recorded in Vicstar. We set out below a flowchart of the arrangement based on BWI Management's representation.



- (a) The purchase and sales figures recorded in Vicstar represent Vicstar's purchases from the import agents and the sales orders in the CRM system for the China market respectively. This was a back-to-back arrangement in which every sale from BWI to the import agent would be on-sold by the import agent to Vicstar at a mark-up (i.e. Vicstar's purchases). When the distributors in China purchase the products, the sales order is keyed into the CRM system and the import agent will arrange for the distribution of the products, as well as collection of monies from such sales.
- (b) Vicstar also records commission expenses in its financials. The import agent will facilitate the payment of commissions to the China distributors and the balance, which represents collections net of commission payments and monies due to the import agents, are ultimately transferred back to Vicstar¹⁰.

¹⁰ We understand that it is on this basis that Vicstar receives money from Changsha Best.

35. While we were informed that this was the arrangement between the import agents and Vicstar, we note from third-party delivery documents that the goods were physically delivered from BWI directly to the import agents in China. We are unable to establish the commercial rationale of this back-to-back arrangement which appears inconsistent with the substance of the underlying transaction. We have not sighted any agreements between Vicstar and Changsha Best on the arrangement. BWI Management was not able to explain the basis or rationale for which these transactions/ activities were recorded in the financials of Vicstar. In our view, the financial statements of Vicstar does not accurately reflect the true commercial substance of the activities in Vicstar.

Cash movement analysis of Vicstar

36. From our cash movement analysis based on Vicstar's bank statements from 1 January 2017 to 31 March 2020, we noted significant cash inflows of SGD16.8 million over the period. We were informed that these were transfers from Changsha Best. We were not able to trace these inflows to any supporting documents as we were informed that the transfers were made through money changers. Based on our reconciliation, using estimated average exchange rates¹¹, we note a difference of SGD543,000 between outflows from Changsha Best and inflows to Vicstar. According to Mr. Yan, this arises from exchange rate differences. However, as there is no documentary evidence¹² on these transfers, we are not able to confirm this.
37. A significant portion of cash outflows amounting to SGD16.5 million was eventually paid to BWI as service fees pursuant to the various service agreement signed between Vicstar and BWI. An amount of SGD2.2 million was also paid to the two shareholders of the company which we were informed represented dividends and directors' fees.
38. As at 31 March 2020, the balance in Vicstar's bank accounts amounted to SGD15,000 and USD127,000 (equivalent to SGD181,000). We have not seen any payments to Mr. Yan for his 70% share of the net profits of Vicstar/ China operations (see paragraph 7(a) above).

Interactions between the Group and Vicstar identified through email reviews

39. As with the import agents, we see similar interactions between the Group and Vicstar in our email reviews. Through these identified interactions, we observe that BWI had assisted in incorporating Vicstar, is substantially involved in the daily operations of Vicstar such as approval of expenses, and also managed the financial affairs of the company including liaising with the external auditors on the financial audit.
40. On 26 November 2019, we interviewed the shareholders of Vicstar to understand its operations and interactions with BWI. Based on our interview, we understand that Vicstar does not have any employees and shares the import agent's local manpower resources. The personnel performing the daily operations and financial activities for Vicstar and assisting to coordinate between the import agents and Vicstar, is an employee of BWI in the Membership Department. We understand that this employee also assists in the preparation of the payment vouchers for the shareholders of Vicstar to approve for disbursement.

¹¹ Average exchange rate obtained from <https://secure.mas.gov.sg/msb/ExchangeRates.aspx>

¹² Third-party documents indicating the amount that is transferred and the respective rate.

41. On 12 June 2020, PwC received a letter from the shareholders of Vicstar to provide clarification on the business relationship between Vicstar, the import agents and the Group. Please see attached letter in Appendix A.

BWI Management's response

42. *Vicstar was initially set up to supply the Group's products in China when the Group was still in the process of obtaining a DSL. Vicstar continued to work with import agents (Qingdao Beihui from 2012 and Changsha Best from 2015) to protect its interests and market share in China.*
43. *Since 2012, Vicstar¹³ became the marketing agent of the Group, handled the CRM system, coordinated training arrangements for the import agents and collected fees on behalf of the Group for non-trade transactions including service fees due to the Group etc., while the import agent was responsible for the operations, importing and distribution of the Group's products to wholesalers in China and also supported transactional inputs for the CRM system which belongs to Vicstar.*
44. *For the Group, such an arrangement would benefit them as in the event of any legal disputes concerning intellectual property rights to the CRM system and payment and collection of monies for the maintenance and operations of the CRM system in China, it would be easier for the Group to enforce its legal rights with respect to Vicstar which is a Singapore legal entity. Vicstar also enabled BWI to charge and collect payments for providing quality control training and media marketing materials for Qingdao Beihui and Changsha Best's China distributors in the form of training and convention events. Vicstar was also responsible for the collections of payments due to BWI from Qingdao Beihui and Changsha Best that reduced BWI's cross border credit risk.*
45. *Since the commencement of its business, Vicstar's books were prepared based on the business records in the CRM system. This served as a means for Vicstar to keep track of the China business transactions. The Group, through Vicstar, monitored the China operations of Qingdao Beihui and Changsha Best. This was achieved by Vicstar maintaining parallel customer and financial records to facilitate the calculation of commissions due to the distributors for all sales in Qingdao Beihui and Changsha Best. The deployment of this CRM system in China via Vicstar was critical for Qingdao Beihui and Changsha Best to develop and support their distribution networks and indirectly the expansion of sales of the Group's products in China.*
46. *Vicstar worked with the import agents as strategic partners to develop the China market via a pricing arrangement. The import agents and their team took charge of all operations in China, including input of transactional records into Vicstar's CRM system. Vicstar would make payments to BWI for other non-trade service fees, as well as reimbursing various third-party fees arranged by the import agents. Such expenses were incurred in China, and thus Vicstar required BWI to assist to validate such expenses before payment.*

¹³ Together with their spouses and their associates.

47. *As the supplier and consultant for both import agents and Vicstar, frequent interactions between Vicstar directors and certain BWI employees were necessary for BWI to provide services to assist both Vicstar and Changsha Best to verify and validate payments. BWI played a role to coordinate and liaise between matters concerning China import agents and Vicstar and performed verification of documents on expenses that were incurred in China as the Vicstar directors had no manpower in China. Save for the above in line with the Group's principal interests, the Group did not interfere and was not involved in the private arrangements between Vicstar and the import agents.*
48. *Vicstar played an important role over the past years to continue the Group's difficult journey to develop the China market. Without the joint efforts of the import agents, together with Vicstar and its associates, the Group would not have been able to build up a team of committed and motivated distributors for the Group's products in China over the past years. Thus, the China market built up by Vicstar and the import agents benefitted BWI in growing the turnover sales of the Group's in the China market over the years.*
49. *With the commencement of the Franchise Model from July 2018, Vicstar ceased the arrangements with the import agents. Franchisees continued to work with Vicstar till June 2019 to compute commissions as the CRM system previously used by Vicstar and the import agents had sales records which facilitated the computation of commissions payable to the distributors based on the algorithm calculations formatted by the CRM system. The Group and its controlling shareholders do not have any pecuniary or beneficial interests in Vicstar nor is Vicstar in any way under the control of the Group, in any respect whatsoever. All the monies in the bank accounts of Vicstar belong to Vicstar which is wholly-owned by its shareholders. The shareholders of Vicstar have confirmed in no uncertain terms that no monies therein are due to or belong to BWI or the management shareholders of BWI.*

PwC's Observation

50. From the corporate profile searches, it would appear that Vicstar is a separate legal entity from the Group, with its registered owners independent from the Group's management.
51. Nonetheless, from our observations of Vicstar's processes and controls through the review of digital evidence, it appears that the Group has been managing the financial affairs of Vicstar. The roles played in transaction approval and business decision making appears to be beyond the capacity of an advisor as defined in the service agreements between both parties.
52. We understand that there are no employees in Vicstar. The operations of Vicstar appear to be managed by BWI employees. While we note BWI Management's response that Vicstar's operations in China was supported by the import agent's local manpower resources, we are not able to independently verify this. When referring to Vicstar, we are also unable to establish who is the directing mind of Vicstar. During the interview with the shareholders of Vicstar, they have both represented that they do not perform any operational functions except to authorise payments as signatories.

53. While the goods have been sold and delivered from BWI in Singapore directly to the import agent in China i.e. Changsha Best, these goods were subsequently “sold” by Changsha Best to Vicstar in Singapore and then “on-sold” again to China distributors for recording purposes only. Such sales by Changsha Best to Vicstar are not recorded in Changsha Best as we have not seen any official invoices issued by Changsha Best to Vicstar.
54. We are unable to establish the commercial substance of Vicstar’s back-to-back arrangement with Changsha Best. BWI employees assisted in preparing the financials of Vicstar and assisted in liaising with external auditors on behalf of Vicstar. We believe that the financial statements of Vicstar may not accurately reflect the true and commercial substance of the activities of the company.
55. We are not able to understand the actual role played by the shareholders of Vicstar in this set-up. The above circumstances raises concerns whether such arrangement with Vicstar exposes BWI to legal and regulatory risk given the level of involvement of BWI in managing this entity.
56. While this is not within the scope of our work, we strongly recommend that the Board seek legal advice on the implications, if any, to BWI. We further recommend that the Group’s external auditors consider the implications, if any, of the above arrangement to the Group’s financial statements.

Franchise Model

Site visits and interviews with Franchisees

57. As part of our independent review of the Franchise Model, we selected eight Franchisees and performed site visits to verify the existence of the Franchisee’s physical shop front. These site visits were arranged for us by BW Changsha. We interviewed the Franchisee owner¹⁴ to understand the operational process of sales and purchases of the Franchisee.
58. From our site visits to these eight Franchisees, we observed the following:
 - (a) Franchisees were generally located in buildings with restricted access;
 - (b) There is limited customer traffic during opening hours unless an event and/ or training session has been pre-organised;
 - (c) Franchisees do not have a warehouse to keep stocks and minimal stock is maintained at the premises of the Franchisees; and
 - (d) Contrary to the Franchisee agreement where a Franchisee is required to maintain complete and accurate transaction records, the Franchisees we visited do not appear to have standard book-keeping practices and do not maintain complete financial and sales records.

¹⁴ Of the eight Franchisees visited, two Franchise owners were unable to meet with us and we spoke to the overall operations manager of the Franchisee in those two instances.

59. We performed four additional unscheduled¹⁵ visits to Franchisees and we similarly noted that these Franchisees are located in places which are generally not easily accessible and there were also limited customer traffic while we were there.
60. Based on our discussions with BWI Management and the interviews with the Franchisees, we understand that these shops are not intended to be retail outlets but are used by the Franchisees to host training events/ seminars and product demonstrations for potential customers, as well as a collection point for members to pick up their purchases¹⁶.

Structure of the Franchise Model

61. To operate within the framework of the Franchise License, the Group sought to align the existing sales structure under Changsha Best to fit the Franchise Model. Under the Franchise Model, the Group mapped the seven existing distributor/ member ranks into four tiers i.e. Franchisee, Area Representative (“Area Rep”), Sales Representative (“Sales Rep”) and VIP.
62. The Group entered into franchise agreements with 28 distributors under the Export Model and also entered into contracts with the Area Rep and the Sales Rep. We understand that the types of contracts entered into are not mutually exclusive, and should an individual member be eligible, that member may enter into all three types of contracts with the Group. VIPs do not enter into any contracts with BW Changsha as there are no commissions due to the VIP.
63. While the Group had transitioned into this structure, the manner in which sales are conducted through the member network remained unchanged from the Export Model. Similarly, the basis of commission computation remained the same.
64. BWI Management has informed that the Franchise Model as currently structured is in compliance with local China regulations and the Franchise License. We are unable to comment on the legality of the structure of the Franchise Model under Chinese law and whether it falls within the scope of the Franchise License. In this regard, we have recommended that the Board obtain the advice of an independent and suitably qualified Chinese law expert on these issues, taking into account our findings set out in this section. We understand that BWI Management has since engaged an independent Chinese law firm to provide a legal opinion on the legality of the Group’s present franchise model sales and distribution business under the Franchise Model.

Sales to Franchisees

65. In respect of BWI’s sales to BW Changsha, we did not note any significant exceptions based on the work performed on the samples selected. We traced the sales and movement of goods from BWI to BW Changsha during the Franchise Model period to third-party documents such as bill of lading on a sampling basis. We also traced payments for these goods to BWI and BW Changsha’s bank statements. As mentioned in paragraph 9, we further performed a throughput analysis of the “DR’s Secret” SKU from the quantity of raw materials purchased by BWI to the quantity of finished goods sold to BW Changsha.

¹⁵ These were “surprise” visits conducted by PwC without prior arrangement with BW Changsha.

¹⁶ We note from third-party delivery documents that the goods are either delivered to the Franchisees or directly to members.

66. In respect of BW Changsha's sales to Franchisees, we traced the sales recorded in BW Changsha's financials to significant Franchisees on a sampling basis for the period of 1 June 2018 to 31 December 2018, to underlying invoices, delivery instructions, third-party warehouse records and confirmation from the third-party logistics providers. As part of our throughput analysis, we also attempted to reconcile purchases from BWI and sales to Franchisees with BW Changsha's inventory balance as at 31 December 2018. We set out below our findings.

Goods sold but remain undelivered in the third-party warehouse

67. As part of our samples testing on inventory and sales to significant Franchisees, we noted undelivered goods with an estimated value of approximately CNY111.8 million¹⁷ (equivalent to SGD22.2 million) as at 31 December 2018. As members have already paid, their goods were recorded as sold in FY2018 even though it was still at the third-party warehouse. Based on the records of the third-party warehouse, these goods were subsequently delivered in 2019.
68. BWI Management has performed a subsequent review of all sales to Franchisees and represented that the estimated value of undelivered goods as at 31 December 2018 is approximately CNY54 million (equivalent to SGD10.7 million). We were informed by BWI Management that the differences arose due to the incomplete information in the confirmation provided to us by the third-party logistics provider which had omitted deliveries from 25 December 2018 to 31 December 2018. While we have requested for and received a second confirmation from the third-party logistics providers, we are not able to reconcile the differences through any independent testing.
69. As this is not part of the scope of the independent review, we recommend that BWI's external auditors review the computations of BWI's Management and consider the adjustments which ought to be made to the sales and inventory numbers for the financial year ended 31 December 2018.

Potential understatement of sales and expenses

70. We note from our testing of BW Changsha's sales to its Franchisees that BW Changsha had recognised approximately 80% of the sales value based on the 发票 ("fapiao") issued¹⁸. However, members pay 100% of the sales value. In our cash receipts testing, we note that proceeds of approximately 20% of the sales value had been deposited into the personal bank accounts of individuals. Some of these accounts are the same as those mentioned at paragraph 13.
71. Given that the personal bank accounts during the Export Model period continued to be used by BW Changsha, we are unable to determine how much of the cash in these accounts belong to BW Changsha or Changsha Best. We are also unable to establish if payments made from these accounts relate to BW Changsha or Changsha Best. Based on our work to date, we note that the outflows from these personal bank accounts include commission payments to members, payments to employees as well as transfers to Vicstar.

¹⁷ Based on the quantity undelivered as confirmed by the third-party logistics provider at the average price sold by BW Changsha during FY2018.

¹⁸ The fapiao is at 80% of the selling price to members. A fapiao is an official invoice issued by the Chinese Tax Bureau (but provided by the seller) for any goods or services purchased within the country. The Chinese government uses these invoices to track tax payments.

Cash movement analysis of the personal bank accounts

72. From our cash movement analysis from 1 July 2018 to 31 March 2020, we note the following:
- (a) A total of approximately CNY397.8 million (equivalent to SGD78.8 million) cash inflows relating to sales and approximately CNY385.1 million (equivalent to SGD76.3 million) cash outflows relating to commission were not recorded in BW Changsha's financial records;
 - (b) A total of approximately CNY29.1 million (equivalent to SGD5.8 million) of transfers to Vicstar. Together with approximately CNY56.1 million (equivalent to SGD11.5 million) of transfers to Vicstar from the personal bank accounts during the Export Model period i.e. 1 January 2017 to 30 June 2018, we note a total of approximately CNY85.2 million (equivalent to SGD17.3 million) of transfers to Vicstar; and
 - (c) A total of approximately CNY63.2 million (equivalent to SGD12.5 million) cash outflows pertaining to payments to employees of BW Changsha, which appears to be sales incentives. BWI Management has informed that these payments are in relation to severance payments, bonus payments and payments to Mr. Yan in respect of Changsha Best's operations and that such payouts took place after July 2018. We are unable to establish if such payments relate to Changsha Best or BW Changsha as these payments are made to the same individuals who are currently BW Changsha employees. We are also unable to independently verify the ultimate recipient(s) of these payments as most payments are made by way of cash.

Summary of cash payment to Vicstar, the import agents, and BWI, arising from BWI's business relationship with these parties

73. Based on our work over the cash movement of Changsha Best, Vicstar and the personal bank accounts, we summarise below the total cash paid out to BWI, the shareholders of Vicstar, Mr. Yan and BW Changsha/ Changsha Best employees during the period from 1 January 2017 to 31 March 2020¹⁹:

Categories	SGD (‘000)	CNY (‘000)	Total amounts (translated to SGD)	As a percentage of total payments
Payment to BWI	(16,490)	(41,998)	(24,951)	52.1%
- Royalty fee from Changsha Best	-	(41,998)		
- Service fee from Vicstar	(10,884)	-		
- Other payments from Vicstar	(5,606)	-		
Payment to Vicstar shareholders	(2,173)	-	(2,173)	4.5%
Payment to Mr. Yan and employees of BW Changsha/ Changsha Best	-	(103,144)	(20,780)	43.4%

¹⁹ These payments exclude commission payments made to distributors/ members and other operating expenses. Apart from the payments made to BWI, none of the other payments can be verified to underlying source documents to independently establish the basis of payment. As most of the payments to Mr. Yan and the employees are paid by way of cash, we are also unable to confirm the ultimate recipient(s) of the funds.

74. In summary, from the business arrangement between BWI, Vicstar and the import agents, our analysis shows that approximately SGD24.9 million or 52.1% of the residual cash²⁰ was paid to BWI in the form of royalty fees, service fees and expense reimbursements. Approximately SGD20.8 million or 43.4% of the remaining cash appears to have been paid to Mr. Yan and BW Changsha/ Changsha Best employees. The remaining balance of SGD2.2 million appears to have been paid to the shareholders of Vicstar. We have not seen any direct payments made to Mr. Koh KC²¹.
75. Except for the payments to BWI, which is supported by service agreements and traced to bank statements, there are no underlying records to document the basis of the amounts paid to the other parties. Other than the payments made to BWI, we are unable to independently verify the ultimate recipient(s) of the funds. We are not able to comment on whether this benefit sharing arrangement between BWI with Vicstar and the import agent, Mr. Yan and the employees, fairly reflects and commensurate with the underlying services performed by each respective party.

BWI Management's response

76. *During 2018, BWI set up BW Changsha with the intention to take over the entire China business as anticipated by Mr. Yan and his employees. To smoothen the transition, BW Changsha hired the entire Changsha Best sales team set up by Mr. Yan as the team was very experienced and already had an established and successful track record in promoting the Group's products in China. The Group was of the belief that doing so would ensure minimal disruption to operations on the ground. In addition, the Group would not need to acquire Changsha Best and assume the risks and liabilities associated with the acquisition of a foreign corporate entity.*
77. *Without a limited transition period, it would have been difficult and highly disruptive for Mr. Yan and his team to join BW Changsha. As such, BW Changsha agreed with Mr. Yan and his distributors to a one-year transition period starting from 1 July 2018. Under the Franchise Model, BW Changsha would deal with Franchisees directly. During the transition period, BW Changsha would sell products to the Franchisees at the franchise price, i.e. approximately 80% of the recommended retail price. The Franchisees would on-sell the products to the Sales Rep (also consisting of Area Rep) at the recommended retail prices of the respective products, giving the Franchisees a margin of approximately 20% as trade rebates. The Franchisees would then pay the commissions directly to the Sales Rep/ Area Rep with their 20% margin via the private payment arrangements set up by Mr. Yan.*

²⁰ Net of sales and purchase of goods, commissions to distributors/ members, and other operating expenses.

²¹ We were informed by BWI Management that Mr. Koh KC received the return of his capital in March 2020 (please see paragraph 16 above).

78. *Mr. Yan was at all times in total control of the payment arrangements and the personal bank accounts. These accounts were opened in the names of individuals whom he had met and became acquainted while attending the BWI annual convention. Save for the three bank accounts opened in the name of the spouse of a BWI employee, none of the individuals are employees of the Group, have direct or indirect relationship with the directors, key management or controlling shareholders of the Group, or an associate of such key director, key management or controlling shareholders. Mr. Yan or his staff approached these individuals to facilitate the opening of bank accounts under their personal arrangements.*
79. *Mr. Yan has confirmed in writing that the monies collected from the Franchisees via Mr. Yan's private arrangement represents the trade rebates enjoyed by the Franchisees. Accordingly, such monies do not belong to BW Changsha or the Group. In addition, the commissions paid from these personal bank accounts are not the responsibility of BW Changsha, as there are no contractual agreements between BW Changsha or the Group and distributors to pay such commissions. As such, these transactions should not be recorded in the books of BW Changsha, as the Group had no legal interest in such monies or any legal obligations in respect of managing its use.*
80. *It was the intention that under the Franchise Model, a payment gateway would ultimately be implemented to assist Franchisees with payments of commissions due to their distributors. However, the Franchisees and the distributors required a transition period to work out their respective payment arrangements.*
81. *The transition period with the Franchisees ended on 30 June 2019. Pursuant to the end of the transition period, Franchisees now pay 100% of the recommended retail price, and BW Changsha now pays marketing fees (which represent the previous trade rebates) and this approximate 20% of the recommended retail price. The Group implemented payment gateway solutions to manage these marketing fees payable to the distributors. These payment gateways, which provide payment solutions to individuals/ businesses, are service providers licensed by the 中國人民銀行 (People's Bank of China). To the best of BWI Management's knowledge, the private payment arrangements of Mr. Yan are no longer in use after all the Franchisees' obligations have been fulfilled by Mr. Yan. All remaining amounts owing to and from Franchisees were fully settled within a few months after the end of the transition period.*
82. *Mr. Yan has confirmed in writing that all balance monies in the bank accounts do not belong to the Group. The monies were mainly the surplus monies from Changsha Best operations and would be used to settle his obligations to his employees as severance payments and bonus payments for past performance in Changsha Best. All other remaining monies would be his share of profits from past operations, to be shared with his key management and his strategic partners.*
83. *The commissions paid during the Franchise Model were structured with legal advice (through meetings and discussions) prior to commencement of the Franchise Model in June 2018. BWI had previously obtained legal opinion from a reputable law firm in China to advise that the Group's payment of commissions to their Franchisees, Area Rep and Sales Rep are permissible within China laws and regulations.*

84. *During the period from 1 July 2018 to 31 March 2020, the monies collected in the personal bank accounts via Mr. Yan’s private payment arrangement relate to receipts from sales, which approximates 20% of recommended retail price of products sold, as trade rebates. These monies were mainly paid as commissions and some IT service fees rendered by BWI for the computation of the commissions. As such, there were no balances remaining from the 20% trade rebates in any of the personal bank accounts. The monies paid out to the employees represent employee’s severance payments and bonus payments for their performance in Changsha Best, as well as payments to Mr. Yan in respect of share of profits from Changsha Best operations. These were paid substantially from the brought forward surplus cash from Changsha Best operations.*

PwC’s Observation

85. Based on our work, it is noted that even after the change to the Franchise Model, the practice of channelling sales receipts to the personal bank accounts continued. While BW Changsha had recognised approximately 80% of the sales value based on the fapiao issued²², members pay 100% of the sales value. While we note BWI Management’s explanation that these monies in the personal bank accounts represent the Franchisee’s trade rebates and belong to the Franchisees, based on our work, it appears that these accounts were used not only to pay commission earned by members but also to make various payments to employees. We have not seen evidence to support the position or claim that these monies belong to the Franchisees.
86. BWI Management stated that the personal bank accounts continued to be used to pay employees²³ in relation to Changsha Best’s operations even after June 2019 as outstanding amounts owing to Changsha Best could only be reconciled at the end of the transition period i.e. 30 June 2019. We are unable to independently verify this to any supporting source documents. Most of the amounts withdrawn for Mr. Yan and BW Changsha employees are made out in cash.
87. As funds in the personal bank accounts are co-mingled, it is not possible to identify or quantify how much of it belongs to BW Changsha. The practice of recording transactions outside of BW Changsha’s official records is a concern. In our view, from a financial perspective, all cash movements relating to BW Changsha should be fully and accurately recorded in BW Changsha’s books i.e. total sales revenue and any corresponding trade rebates, commission expenses or incentive payments to employees should be fully recorded as BW Changsha’s income and expenses. The Balance Sheet should then record the corresponding rebate or commission payables, receivables and cash. Section 199 of the Singapore Companies Act, Cap. 50 states that: *“Every company shall cause to be kept such accounting and other records as will sufficiently explain the transactions and financial position of the company and enable true and fair financial statements”*. BWI Management should obtain legal advice on whether the manner in which these transactions have been recorded in the Group and BW Changsha is in compliance with this section of the Singapore Companies Act.

²² The fapiao is at 80% of the selling price to members.

²³ At the end of the Export Model period, the employees of Changsha Best were employed by BW Changsha.

88. In addition, we understand that none of the AC were aware of the true nature of these transactions, how these transactions had been recorded nor the existence of personal bank accounts referred to above. It appears that BWI Management's decisions and actions on the matter were never tabled to the Board for deliberation and approval.
89. Our scope of work does not include a review of the accounting treatment for transactions. We recommend that the Board work with the Group's auditors to review and consider if any reclassification or adjustments are necessary to the financial statements for the years 31 December 2018 and 31 December 2019 to ensure that BWI's records represent a complete and accurate view of its financial affairs.
90. We further recommend that the Board seeks a formal legal opinion on the above to understand the legal and regulatory implications and/ or consequences.

Corporate Governance and Compliance with SGX listing rules and Other Regulations

91. In the event the sales and expenses of BW Changsha have not been fully recorded, this may constitute a breach of:
 - (a) Section 199 (1) and 199 (2A) of the Companies Act which requires companies to keep accounting and other records to sufficiently explain the transactions and financial position of the company and to maintain an adequate system of internal accounting controls to provide reasonable assurance that assets are safeguarded and transactions recorded;
 - (b) Rule 703 of the SGX Listing Rules which require companies to announce information that may affect the price or value of its securities; and
 - (c) Rule 719(1) of the SGX Listing Rules which require companies to have adequate and effective internal controls and risk management system.
92. We recommend that the Board seeks legal advice on the implications of the above potential breaches and thereafter take the necessary remedial action.
93. We have considered our findings in light of the 2012 Code of Corporate Governance (the "Code") and the 2018 Code of Corporate Governance²⁴ (the "Revised Code"). Under the Code, the Company is required to comply with or explain if there is any deviation from the Code. Under the Revised Code, it is mandatory for the Company to comply with the Principles and explain any deviations from the Provisions of the Revised Code.
94. Based on our findings, the Group may be required to explain if they have deviated from Principle 6, 10 and 11 of the Code, and Provision 1.6 of the Revised Code. The Group may also be in potential breach of Principle 9 of the Revised Code. These Principles and Provisions set out the responsibilities of the Management and the Board over the company's operations and finances.

²⁴ The 2012 Code of Corporate Governance has been replaced by the 2018 Code of Corporate Governance which came into effect from 1 January 2019.

95. In light of the circumstances, we recommend that the AC undertakes the following immediately:
- (a) A comprehensive risk assessment to identify all potential legal, financial and business risk faced by the Group. The AC should formulate an action plan on such risks identified;
 - (b) A thorough review of the Group's corporate governance, legal and compliance process and to put in place formal policies moving forward. The AC should consider appointing a senior compliance officer reporting directly to the AC to implement any agreed remedial actions and to take all necessary steps to oversee the compliance function; and
 - (c) A thorough review of the overall corporate structure of the Group to identify if similar structures exist in the Group and ensure that these are in compliance with local and Singapore regulations.

Internal Controls

96. While our scope of work does not include a detailed internal control review over all processes, we highlight below weaknesses identified in performing our work over BW Changsha's sales processes:

- (a) *Lack of contemporaneous documents*

Franchisees place orders with BW Changsha using the order forms which are sent to BW Changsha customer service officers' web-based email address. The order forms are not consistently retained by BW Changsha after the customer service officers enters the purchases into the CRM system. While the CRM system records purchases by each member, the cash collection is centralised and paid by the Franchisee. Without the contemporaneous underlying source documents i.e., Order Forms, we were unable to reconcile the cash receipts to the CRM system. Accordingly, this resulted in the lack of a proper audit trail between the CRM system, the sales order and the cash collection.

We recommend that BW Changsha implements the use of a centralised mailbox to receive the Order Forms placed by the Franchisee and to retain all contemporaneous documents supporting the sales order process and cash receipts in accordance with the local regulation so as to maintain an audit trail to facilitate the verification of transactions and for audit purposes.

- (b) Goods are not delivered on a timely basis

BW Changsha outsources its warehousing and logistics functions to a third-party warehouse. We understand that the third-party warehouse outsources the delivery of goods to a third-party logistics provider. On a monthly basis, the third-party warehouse will issue a fapiao to BW Changsha for the warehousing and logistics services provided. From our review, we did not note any details on the breakdown of the fee other than a fapiao. We understand that the third-party warehouse monitors the deliveries through a tracking sheet, but such information was not provided to us. When we requested for access to delivery documents and tracking sheets, the third-party warehouse informed us that they do not maintain such records and we were denied access.

As at 31 December 2018, there were goods that were recorded by BW Changsha as sales to members even though these goods were only delivered after 31 December 2018. BWI Management represented to us that they were not aware that the third-party warehouse had not directed or requested the third-party logistics provider to deliver the goods as they had assumed that these goods had already been delivered before the end of FY2018.

We recommend that BW Changsha request the third-party warehouse to provide a delivery status update to ensure that all goods sold and recorded as revenue have been duly delivered to members. The third-party warehouse should also retain and provide full access to all delivery documents for audit purposes pursuant to the warehouse agreement.

Limitation of scope

97. Our work and findings in the report are based on the documents that have been made available to us and is subject to the limitations set out below:
- (a) There was no historical financial information available from Qingdao Beihui as the company had been de-registered on 18 February 2019 and no records had been maintained;
 - (b) As part of our work on the import agents, we had requested to meet with the shareholder of Qingdao Beihui, to independently establish the nature of the relationship with the Group. We were informed by BWI Management that the shareholder was unable to meet due to health reasons;
 - (c) We were provided with the profit and loss statements for FY2015 to FY2018 and official fapiao for Changsha Best. Mr. Yan informed that these were for tax filing purposes. No further records for FY2015 to FY2018 were provided. The financial records were incomplete, and no underlying supporting documents were made available;
 - (d) In respect of the personal bank accounts used during the Export Model and Franchise Model period, we were only provided with cash movement spreadsheets from Mr. Yan who informed us that these had been extracted from the personal bank statements. For the personal bank accounts which we were unable to independently verify through online access, we have relied on these cash movement spreadsheets;
 - (e) Cash outflows made through the personal bank accounts lack documentation and are made out in cash. We are not able to independently validate the nature of such payments or the ultimate recipient(s) of the cash;
 - (f) In respect of the bank accounts of Changsha Best, we have relied on the information in these bank statements to categorise the cash movement and have not performed any further work on these cash movements due to the lack of supporting source documents;
 - (g) We were unable to perform a comparison of the margins achieved through the Export Model and the Franchise Model as the funds in the personal bank accounts during the period are co-mingled. It is not possible to independently quantify how much of such funds relate to BW Changsha operations;

- (h) We were only provided with the audited financial statements of Vicstar for FY2015 to FY2018 and selected general ledger accounts without the majority of the underlying supporting documents;
- (i) We were unable to determine if the contracts and agreements by BWI in relation to the China operations (including but not limited to distributorship agreement with the import agents and contracts with the Franchisee, Area Rep and Sales Rep) were on normal commercial terms;
- (j) Most of the arrangements between Vicstar, Qingdao Beihui, Changsha Best, and the Franchisees are as represented by BWI Management or Mr. Yan. We are not able to corroborate their representations independently as we were informed these were oral arrangements;
- (k) We were provided with limited records from the Franchisees which made it difficult for us to perform any meaningful verification work on them; and
- (l) We were not able to retrieve data from the laptops of individuals in China as these were either not available, found to be faulty or had no usable data on them. In performing our work, we relied mainly on data residing in the email servers that we were able to obtain.

Disclaimer

- 98. PwC has not been asked to (and it has not) comment on, review or assess the validity or enforceability of the documents provided to PwC. The procedures that PwC performed under this engagement do not constitute an audit or review in accordance with generally accepted auditing or attestation standards. PwC has not audited or otherwise verified the information supplied to it in connection with its work from whatever source except as specified herein.
- 99. PwC's findings are based on documents and information relevant to its scope of work that were made available to PwC up to 23 July 2020. Documents or information provided to PwC after 23 July 2020 may have an impact on the Report. PwC reserves its right to correct any part of its findings as and when such documents or information emerge.
- 100. PwC makes no representation and gives no warranty to any person (except to the extent provided in our engagement letter dated 18 March 2019 and addendum letter dated 28 June 2019 (together, the "Contract")) as to the accuracy or completeness of the Report. Similarly, PwC does not accept or assume responsibility for its work and the Report to any other party (except as specified in the Contract). PwC's work was not planned or conducted in contemplation of reliance by any other party. Therefore, items of possible interest to any other party will not be specifically addressed and matters may exist that would be assessed differently by any other party.

Appendix A. - Clarification letter from shareholders of Vicstar

To : PWC

Clarification on Vicstar Lifestyle Matter

We learnt that PWC reported, during the interview, we, the two shareholders of Vicstar Lifestyle (VL) said we knew nothing about the operations and finance of VL, and that all of VL's affairs were handled by BWI's staff. We feel that there were misunderstanding in our communications and therefore wanted to clarify to PWC about the background of VL.

1. The Establishment of Vicstar Lifestyle

- In 2007, which was about the time Best World International (BWI) set up Best World Hunan (BW Hunan) in Changsha, our spouses, together with several other distributors from Singapore, frequently travelled to China to develop the market there. During which, we were able to work with many beauty salons in China to act as our distributors.

In 2009, BWI planned to withdraw from China after its acquisition plan in China fell through.

- Sensing the risk of losing our hard-gained market in the event supply be disrupted, we discussed with BWI management for possible solutions and reached the following consensus; before BWI obtains a China direct sales license, we shall set up a company in Singapore for the purpose of exporting BWI products from Singapore to supply to our distributors in China. As a result, with assistance from BWI staff, we were able to register and set up VL in 2009. Additionally, BWI also introduced us a few staff from their BW Hunan, to assist us in handling operational matters in China. When it came time for BWI to wind up BW Hunan, we decided to take over the company to facilitate the payment of staff salaries and various expenses necessary for our operations in China.
- BWI also designed a CRM system for us. Our China staff would input all business records into this CRM system, which will in turn be used by our third-party bookkeepers to perform their tasks.

2. Cooperation and Partnership with BWI's Export Agent (2012-2018)

- In 2012, one of the distributors from China, Chen Kejun (Chen), called BWI to express his interest to import products directly from BWI to distribute in China. At that stage, Chen's distributors took up half of the China's sales, with the other half achieved by our distributors. Since we really didn't have much time to manage the operations in China, we thought it could be better if someone were to take over the import and supply chain operations. However, our spouses and fellow distributors primary concern was the possibility of a competing party being able to gain access to our client database. In the event should the new agent implement their own CRM system or, even worse, represent another line of products, all our clients could potentially be poached.

With assistance rendered by BWI management, VL and Chen's Qingdao Bei Hui (QDBH) eventually reached a consensus to work as partners to jointly develop the Chinese market.

- Around 2014 and 2015, as a result of Chen's health issues, then marketing manager of QDBH, Yan Weijun (Yan), took the initiative to set up Changsha Bai Shi Te Wei (Changsha BSTW) to replace QDBH's role as the agent of BWI. VL continued to work in partnership with Yan's Changsha BSTW.

3. Partnership Model between VL and the Two Export Agents

- The Export Agents imported BWI products and made payments directly to BWI.
- The Export Agents supplied to beauty salons in China through VL's CRM system. VL on the other hand received payments from distributors and, after deducting rebates/commissions to distributors, made payments to the Export Agents at wholesale price (45% to 50% of the selling price) for the goods sold. The Export Agents were in charge of all operating expenses in China, including staff salaries and payments to BWI.
- The staff of the Export Agents assisted VL to handle all operational matters, including the entry of all business transaction records into VL's CRM system, the issuance of rebates/commissions to distributors and the remittance of the balance to VL.
- As practiced previously, VL's accounts were prepared based on the business records in the CRM system. This served as the means for us to keep track of China's business transactions.
- VL made payments to BWI for other non-trade service fees, which include maintenance of the CRM system, training, branding consultancy, etc., as well as reimbursing various overseas third-party fees, such as the trainers' fees, media production and convention's expenses. All third-party fees will be paid by cheque under the arrangement and acknowledgment by the Export Agents' management, as well as after verification by the BWI's staff.
- The verification by BWI's staff serves as a neutral third-party verification which was necessary as we are not physically present in China to be completely sure that all payments are made in good order. BWI's verifications reassured us in that respect and BWI were paid fees for these services.
- The partnership between VL and the Export Agents was mainly to ensure that our distributors in China can enjoy uninterrupted supply of products and uninterrupted growth in the China market, before BWI takes over.
- We reached an agreement with Yan that, at any point when BWI takes over the market, upon settlement of all the accounts, the remaining surplus will be split 70:30 between Yan & team, and us respectively. Although we did not enter into any formal agreement on this matter, we feel that Yan had already allocated the respective profit margins when establishing the wholesale price that VL has to pay Changsha BSTW.
- As all operations matters were under the charge of Yan and his team, and based on the very limited responsibilities we hold, we are both agreeable that it was reasonable that Yan and his team get to receive 70% of the surplus.

4. Others

- Although the two of us rarely participated in the operations in China, our spouses and several of their Singapore distributors devoted effort on a daily basis in the development of the Chinese market, especially in the areas of distributors' training and the development of beauty salons from all over China to distribute our products. The steady growth of China market is largely attributable to our effort over these years. And the existence of VL and its continued partnership with the Export Agents serves to reassure us that our effort, our interests and our benefits, present and future, are being well protected.

- While Yan and we were mentally prepared for BWI to take over the Chinese operations any time after obtaining their direct selling license in 2016, this did not happen until they obtained a franchise permit in mid-2018. Our only requirements to BWI is that BWI must take over all balance inventory and hire all staff of the Agent.
- While we may not be personally involved with the business, we were very confident of the business as Yan and his team fully took charge of day-to-day affairs and business operations, with business performance being tracked by the CRM system which were verified by BWI. Last but not least, our spouses and several other Singapore distributors are personally involved in market development and distributors training. As such, when being questioned by PwC about the financial or operational details of VL during the interview, we were unable to answer promptly as all operations were handled by Yan and his staff, which forms the basis of VL's partnership with them.
- As a result of weak demand in the earlier years, VL and the Export Agents merely broke even. Since Yan took over the management and introduced sales performance incentives, all staff evidently became highly motivated and involved. Since 2016, performance in China began to improve. With business growth achieved in 2017 and first half of 2018, VL and the Exports Agents were able to enjoy profitability.
- Again, we need to emphasize the pivotal role VL played over the decade to maintain our spouses and several distributors' commitment to continue the arduous task of developing the China market. Without VL, there will be no guarantee that our effort and interest will be protected. And without their effort to development the market, BWI's China business will not be what it is today.
- In mid-2018, when BWI finally took over the Chinese market, we were able to finally withdraw ourselves from the business with the strong belief that the market will be able to enjoy growth from strength to strength as a result of guidance and direct management from BWI.
- At this point, since the audited accounts of both companies were finalized, Changsha BSTW's had been wound up with the bank surplus being fully allocated to Yan and his team. VL is currently also in the midst of being wound up and the bank surplus will be shared by both shareholders. We also have plans to allocate some surplus to Yan as profit sharing when it is possible for him to visit Singapore in the near future.



Koh Lee Cheng
Director / Shareholder
Vicstar Lifestyle Pte. Ltd.
Date: 12/6/20



Chong Keng Seng
Director / Shareholder
Vicstar Lifestyle Pte. Ltd.
Date: 12/6/20