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China Resources Phoenix Healthcare Holdings Company Limited

華潤鳳凰醫療控股有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 1515)

INTERNAL CONTROL REVIEW

References are made to the announcement dated July 8, 2016 and the circular dated October 14, 2016 of the Company. As disclosed in the said announcement and circular, the original annual caps in relation to the Yan Hua IOT Agreement and the PMM Sales Framework Agreement expired on December 31, 2015 and, due to the Company's inadvertent oversight, were not renewed in a timely manner. The new annual caps in relation to the Yan Hua IOT Agreement and the PMM Sales Framework Agreement for the three years ending December 31, 2018 were subsequently approved at the extraordinary general meeting of the Company held on October 31, 2016.

To avoid any similar non-compliance of the connected transaction requirements under Chapter 14A of the Listing Rules and as directed by the Stock Exchange, the Company engaged the Internal Control Adviser to conduct the Review of the Company's internal controls for procuring compliance with Chapter 14A of the Listing Rules of the Group's continuing connected transactions. The written interim report on internal control review has been issued by the Internal Control Adviser and been submitted to the Stock Exchange on October 23, 2017.

METHOD AND PROCEDURES OF THE REVIEW

The Review is conducted by the Internal Control Adviser in accordance with the requirements under Chapter 14A of the Listing Rules.

Set out below is the summary of the procedures implemented by the Internal Control Adviser for the concerned area:

Key Process: Clarify sub-process risk

Policies, procedures and guidelines of the Company: Clarify internal control procedures in accordance with the requirements under Chapter 14A of the Listing Rules

Procedures implemented by the Internal Control Adviser:

- (i) Conducted preliminary review to understand the general information of the Company's internal control and obtained relevant background materials and documents from the Company.

- (ii) Obtained all information of internal control policies, systems and processes in relation to the management of connected transactions and conducted review.
- (iii) Conducted interviews with the relevant management personnel and staff of the Company. Conducted on-site review of the relevant internal control documents at the same time.
- (iv) Conducted walk-through tests on the relevant internal control procedures and systems, in order to confirm the Internal Control Adviser's understanding and whether the Company's internal control operation meets the management's requirements.
- (v) Conducted sample testing on the relevant internal control procedures, in order to confirm if the Company's internal control operation meets the requirements of the management and policy as well as the procedure manual based on the number of samples.
- (vi) Based on the results of the above steps, identified the key defects of internal control and made appropriate improvement recommendations.

FINDINGS AND IMPROVEMENT RECOMMENDATIONS OF THE REVIEW

Issues regarding the design of review process on identifying new connected persons

Summary

In the qualification checklist of new suppliers, there is no checkbox provided to indicate the review results as to whether it is a connected person. Therefore, some of the Company's subsidiaries/hospitals left no record when reviewing if there is any potential new connected person.

As the Company was gradually promoting the top-down supply chain management system, and the supplier groups in the pharmaceutical industry were relatively stable with sufficient information disclosure, it is understood that the Company did not identify new connected persons under the bottom-up approach in the recent two years.

As noted from the interviews, the Group's supply chain department would verify if there is new connected person during the qualification review on new business partners, and the Group's finance department would meet with the Board office and external counsels to confirm if they are connected persons. However, the "Implementation Rules for the Management of Connected Transactions (《關連交易管理實施細則》)" did not clearly outline the specific steps for the Group's supply chain and other relevant departments to identify new connected persons, and there is no checkbox provided in the qualification checklist of new suppliers to indicate the review results as to whether it is a connected person. Therefore, some of the Company's subsidiaries/hospitals left no record when reviewing if there is any potential new connected person.

Impact

As the design of review process on identifying new connected persons did not clearly outline the specific steps, there was no record left during some of the review processes, which gave rise to the possibility that new connected persons may not be identified in a timely manner.

Improvement Recommendations

The specific steps for identifying new connected persons by the relevant departments of the Group's supply chain stipulated in the "Implementation Rules for the Management of Connected Transactions" shall be improved, or the relevant checklist for the acceptance of business partners shall be redesigned, in order to maintain the review records in relation to the inspection on whether there is new connected person by the relevant departments and file them for further inspection.

Response from the Company

The responsibilities and processes of review of the suppliers will be improved and added in the "Implementation Rules for the Management of Connected Transactions". The supply chain management department will add the content in respect of whether a supplier is a connected person in the qualification checklist of new suppliers after review, in order to specify the review processes and maintain the review record. The list of suppliers of the supply chain for the current month will be reviewed at the end of the month and the connected persons will be clearly marked, in order to guarantee the identification of both existing and new suppliers and maintain the review record.

Issues regarding the reconciliation management of connected transactions

Summary

As the Company did not standardize a unified method for reconciliation of the connected transactions under its system, reconciliation management was set up based on the specific circumstances of the Company's subsidiaries/hospitals. Some of the Company's subsidiaries/hospitals did not keep daily written reconciliation records. For example:

- (1) Wugang Hospital: Connected persons conducted on-site verification of physical accounts and financial accounts of connected transactions with the business personnel and financial officers of Wugang Hospital, respectively, from time to time, but no regular reconciliation records are maintained;
- (2) Xukuang Hospital and Jian Gong Hospital: Connected persons conducted reconciliation with the pharmaceutical departments of the hospitals verbally or by phone on a monthly basis, but no regular reconciliation records are maintained;
- (3) Huaikuang Hospital: Reconciliation was conducted verbally, by phone and in writing, and regular reconciliation records are maintained; and
- (4) Beijing Wanrong and Beijing Jiayi: Reconciliation was conducted by phone before payment or conducted based on delivery orders or the confirmation issued by connected persons.

Impact

As there was no unified standard for reconciliation management of connected transactions, it could not be guaranteed that the daily reconciliation of connected transactions would be carried out on time and strictly executed, which may cause the value of connected transaction to be inaccurate and affect the accuracy of the daily statistics of connected transactions.

Improvement Recommendations

Method and requirements for reconciliation of the connected transactions should be specified under the internal control system. Each of the Company's subsidiaries/hospitals should carry out written reconciliation with connected persons on a regular basis, which should at least verify the connected transaction accounts with connected persons on a quarterly basis and fully record the reconciliation period, reconciliation amount and reconciliation person as well as keep the reconciliation checklists confirmed by both parties. If any reconciliation discrepancy is found, the case should be timely handled to ensure reconciliation consistency between the accounting records of both parties.

Response from the Company

The Company shall improve the Implementation Rules for the Management of Connected Transactions, as to the reconciliation of the connected transactions of the Company and its subsidiaries/hospitals, maintain a clear procedure for such purpose and require the parties to maintain the relevant reconciliation records for inspection. The financial departments or relevant departments of the Company and its subsidiaries shall conduct reconciliation between the value of connected transactions and outstanding account receivables with connected persons at the end of each month and year, and maintain the relevant reconciliation records by email or in written form.

Issues regarding the management of connected transaction agreements

Summary

The subsidiaries/hospitals of the Group within the scope of testing have not fully implemented the marking requirements for connected transaction agreements.

Pursuant to the "Implementation Rules for the Management of Connected Transactions" formulated by the Company, the subsidiaries/hospitals shall mark the wordings "connected transactions" on the connected transaction agreements and establish ledgers for such transactions in which all information shall be recorded in a timely manner, and a "Monthly Report of Connected Transactions (關連交易月報表)" shall be submitted in due course within the first five days of each month.

According to the interviews, the subsidiaries/hospitals within the scope of testing have not implemented the requirements of the rules to mark the wordings "connected transactions" on the connected transaction agreements. It is noted from the texts of the connected transaction agreements, as collected on sampling basis, of the subsidiaries/hospitals which had entered into such agreements during the testing period, the connected transaction agreements of the headquarters, Brain Hospital and Beijing Jiayi have not been marked with the wordings "connected transactions".

The maintenance of the connected transaction orders is system-based and the subsidiaries/hospitals made payments for the orders of connected persons for the current period by sorting the information with agreed credit term. Currently, the actual number of connected persons of the subsidiaries/hospitals is relative low, so the risks in relation to statistical errors of connected transaction information and miscalculation of the amount of payment for connected transactions are relatively low at this stage. However, with the increases in the number of connected persons as well as the type and amount of connected transactions in the future, further improvement in respect to the connected transactions control system has to be made.

Impact

Failure to manage connected transaction agreements in accordance with the Company's unified requirements may pose negative impacts on the standardization and unified management of connected transactions. In addition, with the increases in the number of connected persons as well as the type and value of connected transactions in the future, the completeness of the statistics in relation to the connected transactions may be affected.

Improvement Recommendations

Each of the subsidiaries/hospitals of the Group is recommended to manage connected transactions in strict compliance with the relevant requirements given by the companies at a higher level and mark the wordings "connected transactions" on connected transaction agreements. The connected transactions management department of the Company should carry out regular inspection on the implementation of the connected transactions rules by the subsidiaries in order to ensure full implementation of all requirements.

Response from the Company

The form of marking on the connected transaction contracts will be unified and standardized by the headquarters and all existing connected transaction contracts as well as new contracts which are still at the approval stage will be marked accordingly. The finance department of the Company and its subsidiaries will review the list of suppliers at the end of each month in order to ensure the completeness of the identification and statistics of connected persons, the results of which will then be reported to the supply chain management department of the Group. Should there be any abnormalities, the finance department of the Company's subsidiaries will notify the finance department of the Group in a timely manner to update the statistics in relation to the connected persons.

The Company agrees with the Internal Control Adviser that the above findings represent areas of improvement in the Company's internal control in relation to compliance with Chapter 14A of the Listing Rules and the Company has undertaken to implement the relevant recommendations of the Internal Control Adviser within 2 months after the date of the written interim report on internal control review of the Internal Control Adviser (i.e. by December 23, 2017) and publish a further announcement within 2 weeks thereafter of its full implementation of the recommendations.

DEFINITIONS

In this announcement, unless the context otherwise requires, the following expressions have the following meanings:

“Beijing Jiayi”	Beijing Phoenix Jiayi Medical Equipment Company Limited* (北京鳳凰佳益醫療器械有限公司), a wholly-owned subsidiary of the Company principally engaged in the business of medical equipment supply chain;
“Beijing Wanrong”	Beijing Wanrong Yikang Pharmaceutical Company Limited* (北京萬榮億康醫藥有限公司), a wholly-owned subsidiary of the Company principally engaged in the business of pharmaceutical supply chain;

“Board”	the board of Directors;
“Brain Hospital”	Guangdong 999 Brain Hospital* (廣東三九腦科醫院);
“Company”	China Resources Phoenix Healthcare Holdings Company Limited, a company incorporated in the Cayman Islands with limited liability, the shares of which are listed on the Main Board of the Stock Exchange;
“connected person(s)”	has the meaning ascribed to it under the Listing Rules;
“Director(s)”	the director(s) of the Company;
“Group”	the Company and its subsidiaries;
“Huaikuang Hospital”	Huaibei Miner General Hospital* (淮北礦工總醫院);
“Internal Control Adviser”	an independent internal control adviser engaged by the Company to conduct the Review for procuring compliance with Chapter 14A of the Listing Rules of the Group’s continuing connected transactions;
“Listing Rules”	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited;
“PMM Sales Framework Agreement”	the pharmaceutical, medical device and medical consumables sales framework agreement dated November 6, 2013, supplemented by the supplemental agreement dated July 8, 2016, entered into between the Group and Yan Hua Hospital;
“Review”	the review of the Company’s internal controls for procuring compliance with Chapter 14A of the Listing Rules of the Group’s continuing connected transactions conducted by the Internal Control Adviser;
“Stock Exchange”	The Stock Exchange of Hong Kong Limited;
“subsidiary”	has the meaning given to it under the Listing Rules;
“Wugang Hospital”	China Resources Wugang General Hospital* (華潤武鋼總醫院);
“Xukuang Hospital”	Xuzhou Mining Hospital* (徐州市礦山醫院);
“Yan Hua Hospital”	Yan Hua Hospital* (北京燕化醫院); and

“Yan Hua IOT Agreement” collectively, the hospital management right and investment framework agreement dated February 1, 2008, and the hospital investment management agreement dated February 4, 2008, both of which were supplemented in April 2008, December 2010, June 2011, June 2013, July 2013, September 2013 and October 2013, and were entered into between the Group and Yan Hua Hospital.

* *For identification purpose only*

By Order of the Board
China Resources Phoenix Healthcare Holdings Company Limited
HAN Yuewei
Executive Director & Chief Executive Officer

Hong Kong, November 3, 2017

As at the date of this announcement, the Board comprises Mr. WANG Yin and Mr. WANG Yan as non-executive Directors; Mr. CHENG Libing, Mr. HAN Yuewei, Ms. REN Yuan and Ms. FU Yanjun as executive Directors; Mr. KWONG Kwok Kong, Ms. CHENG Hong, Mr. SUN Jianhua and Mr. LEE Kar Chung Felix as independent non-executive Directors.