

Hong Kong Exchanges and Clearing Limited and The Stock Exchange of Hong Kong Limited take no responsibility for the contents of this announcement, make no representation as to its accuracy or completeness and expressly disclaim any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this announcement.



第七大道
7ROAD.COM

7Road Holdings Limited

第七大道控股有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 797)

**KEY FINDINGS OF THE INDEPENDENT INVESTIGATION;
AND
UPDATE ON RECENT DEVELOPMENTS
ON SUSPENSION OF TRADING**

This announcement is made by 7Road Holdings Limited (the “**Company**”, together with its subsidiaries, the “**Group**”) pursuant to Rule 13.09 and Rule 13.24A of the Rules (the “**Listing Rules**”) Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) and the Inside Information Provisions (as defined in the Listing Rules) under Part XIVA of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong).

References are made to the announcements (collectively, the “**Announcements**”) of the Company dated (a) 30 March 2020 in relation to (i) the delay in publication of the 2019 Annual Results, (ii) the possible delay in despatch of 2019 Annual Report, (iii) the postponement of Board Meeting, and (iv) the suspension of trading, (b) 10 April 2020 in relation to (i) the change of auditor, (ii) the Unresolved Issues, and (iii) establishment of the Independent Committee, and (c) 12 May 2020 in relation to the Resumption Guidance. Unless otherwise defined, capitalised terms used herein shall have the same meanings as those defined in the Announcements.

BACKGROUND

As disclosed in the Company's announcement dated 10 April 2020, the Board established the Independent Committee, comprising of its independent non-executive Directors to investigate matters relating to the Unresolved Issues on 10 April 2020.

On 17 April 2020, the Independent Committee appointed an independent investigator (the **"Independent Investigator"**) to conduct an independent investigation in respect of the Unresolved Issues (the **"Independent Investigation"**).

On 29 May 2020, the Independent Investigator issued a report of the Independent Investigation to the Independent Committee (the **"Independent Investigation Report"**).

On 3 June 2020, the Independent Committee reported the findings of the Independent Investigation to the Board.

This announcement outlines the key findings of the Independent Investigation and the recommendations made by the Independent Committee.

KEY FINDINGS OF INDEPENDENT INVESTIGATION

The Independent Investigator conducted an independent investigation in respect of the Unresolved Issues.

As disclosed in the Company's announcement dated 10 April 2020, *"During the course of audit and preparation of the 2019 Annual Results, the audit committee of the Company (the **"Audit Committee"**) received a letter from the Auditor on 26 March 2020, in which the Auditor requested the Audit Committee to undertake an independent investigation on two unresolved audit issues (the **"Unresolved Issues"**) in respect of (i) the bonus payment made in cash to a number of research and development staff by Shanghai Xinla Network Technology Co., Ltd. (上海辛辣網絡科技有限公司) (**"Shanghai Xinla"**), an indirectly wholly-owned subsidiary acquired by the Company in 2019, in an amount of approximately RMB6.5 million; and (ii) the prepayment of promotion fees made by 7road International HK Limited (**"7road Hong Kong"**), an indirectly wholly-owned subsidiary of the Company, in an amount of US\$25.0 million to a counterparty (the **"Counterparty"**) under a game cooperation distribution agreement in relation to the advertising and promotion of certain mobile games in the overseas markets."*

Subject to certain limitations, the Independent Investigator made the following key findings:

The 1st Unresolved Issue

1. The 1st Unresolved Issue relates to the payment of cash bonus by Shanghai Xinla to its staff in June 2019.
2. The staff bonus was withdrawn in cash (in relation to a sum of RMB5,875,994) from Shanghai Xinla's account on 27 June 2019. The Independent Investigator found that it was in fact a sum requested by and paid to a former shareholder of Shanghai Xinla (Individual A) for reimbursement of wages paid by Individual A on behalf of Shanghai Xinla in 2018 that were not recorded in Shanghai Xinla's accounts. The staff of Shanghai Xinla did not receive any cash bonus on that day.
3. To establish the legitimacy of the cash withdrawal on 27 June 2019, the human resources manager of Shanghai Xinla (Individual B) produced a document called "Particulars of the Distribution of the 2018 Year-End Bonus" (《2018年度年終獎發放明細》) (the "**Particulars**"), which was approved by the person in charge of Shanghai Xinla (Individual C).
4. The Particulars was fabricated. The information regarding a sum of RMB637,010 being withheld and paid as individual income tax was also incorrect. The management of Shanghai Xinla made inconsistent statements and provided inconsistent explanations about this matter to the former auditor of the Company.
5. Prior to acquiring Shanghai Xinla, the Company had engaged its former auditor to review the accounts of Shanghai Xinla for the years 2016, 2017, 2018 and the first quarter of 2019 and to issue an accountant's report. The former auditor did not issue any qualified opinion in its report on the account of Shanghai Xinla. After the acquisition, Shanghai Xinla submitted its financial accounts to the Company on a monthly basis. No substantial issue was identified in these accounts. The Independent Investigator did not find any evidence suggesting that the Company's management was aware of any off-the-account distributions of subsidies, incentive pay and year-end bonus by Shanghai Xinla.

The 2nd Unresolved Issue

1. The 2nd Unresolved Issue relates to the prepayment of distribution and promotion fees to the Counterparty under a game cooperation distribution agreement.
2. Prior to entering into the game cooperation distribution agreement (the “**Cooperation Distribution Agreement**”) with the Counterparty, the Company evaluated the business models and prepared revenue and expenditure projections for the target games. Based on the results of the evaluations and projections, the Company decided to negotiate and enter into the Cooperation Distribution Agreement with the Counterparty.
3. On 17 January 2019, 7road Hong Kong completed its contract approval process and entered into the Cooperation Distribution Agreement. The Cooperation Distribution Agreement contains terms regarding products under cooperation, cooperation amount, cooperation term, reconciliation and settlement, minimum amount of the monthly distribution fee, criteria of assessment regarding the operation results, gross billings sharing ratio, and minimum corresponding relationship between gross billings and distribution fee. The sharing ratio was in line with the Company’s business strategy, and was subject to a minimum guaranteed return and an agreed distribution period of the target games.
4. After the Cooperation Distribution Agreement was entered into, in view of the actual distribution statistics of the product, 7road Hong Kong believed that it was unlikely the product distribution would meet its expectations. 7road Hong Kong also found out that the Counterparty did not spend at least US\$1.5 million per month on promotion, and did not conduct any assessment of its revenue or pay 7road Hong Kong its share of the profit, in accordance with the Cooperation Distribution Agreement. From the perspectives of business revenue and security of capital, the Company considered that this overseas promotion project was no longer needed. Hence, the director of 7road Hong Kong decided to terminate the Cooperation Distribution Agreement.
5. At the end of June 2019, 7road Hong Kong entered into an agreement for the early termination of the Cooperation Distribution Agreement with the Counterparty. The termination agreement stipulated that the Cooperation Distribution Agreement shall be terminated, and that the Counterparty shall repay a total of US\$26 million to 7road Hong Kong, which consisted of US\$25 million promotion fees prepaid by 7road Hong Kong and US\$1 million for compensation. The Counterparty shall pay US\$11 million, US\$5 million and US\$10 million to 7road Hong Kong by 30 June 2019, 31 July 2019 and 31 August 2019 respectively.

6. During the period between June 2019 and April 2020, 7road Hong Kong took steps to recover payment of the promotion fees of US\$25 million prepaid by it and the compensation from the Counterparty. The Counterparty agreed to pay 7road Hong Kong an additional US\$500,000 as compensation for failing to make timely repayment on multiple occasions. 7road Hong Kong recovered all outstanding promotion fees prepaid by it in the sum of US\$25 million and a compensation in the sum of US\$1.5 million by 9 April 2020.
7. The Independent Investigator made no findings to indicate that (1) the arrangement for the prepayment of the promotion fees by 7road Hong Kong for the target games was against commercial logic; (2) there was a lack of reason for the material changes that happened shortly after the signing of the Cooperation Distribution Agreement between 7road Hong Kong and the Counterparty; and (3) there was a lack of actual supervision or action by 7road Hong Kong for the recovery of the prepaid promotion fees.

INTERNAL CONTROL WEAKNESS IDENTIFIED BY THE INDEPENDENT INVESTIGATOR

The Independent Investigator identified the following internal control weaknesses during the Independent Investigation:

1. There were instances where wages to the staff of Shanghai Xinla were paid off-the-account. Payment of such wages was not recorded in Shanghai Xinla's accounts, and no social security, housing accumulation fund or individual income tax were paid by Shanghai Xinla in respect of such wages.
2. Shanghai Xinla did not formulate a staff handbook nor a written human resources management policy, which resulted in a lack of written policy to regulate the arrangements for payment of wages and year-end bonus. The Company has a written management policy "Measures of financial management of the subsidiaries of 7Road Holdings Limited (Trial)" (《第七大道控股有限公司控股子公司財務管理辦法（試行）》) to monitor its wholly-owned subsidiaries, but the policy has not been fully implemented. The Company did not identify, in a timely manner, that the Company's wholly-owned subsidiary Shanghai Xinla, the acquisition of which was completed on 22 October 2019, paid certain off-the account wages and bonus to its staff.

3. Although the Company has established a monitoring and management system for its subsidiaries, the system is not sufficiently comprehensive. It did not prescribe sufficiently detailed arrangements for the Company's subsidiaries to conduct background checks on a counterparty or its designated third party. It did not formulate any written guidelines regarding the procedures for debt recovery and did not require written records for debt recovery being kept.
4. The Cooperation Distribution Agreement and the related repayment agreements were affixed with 7road Hong Kong's company chop but were not signed. Certain agreements with counterparties were entered into by 7road Hong Kong before completion of its internal approval process.
5. Before entering into the Cooperation Distribution Agreement and making prepayment to the Counterparty, 7road Hong Kong did not conduct a comprehensive and detailed capital risk assessment. It did not adequately assess the potential financial risks of non-recovery of the prepayment, and did not formulate any systematic arrangements for debt recovery.

LIMITATIONS OF THE INDEPENDENT INVESTIGATION

The findings of the Independent Investigator are subject to a specific limitation, which is the failure to obtain supporting evidences, including bank statements and electronic payment records, from the former shareholder of Shanghai Xinla (Individual A) regarding his payment of wages and year-end bonus to staff of Shanghai Xinla.

CONCLUSIONS AND REMEDIAL MEASURES

The Independent Committee has carefully considered the findings of the Independent Investigator and endorsed the same.

The Independent Committee has the following observations and recommendations on the remedial measures:

1. The Independent Committee considers that it was wrong for Individual B and Individual C to produce the Particulars and withdraw cash in the amount of RMB5,875,994 from Shanghai Xinla's bank account for payment to the former shareholder of Shanghai Xinla, Individual A, on the basis of the Particulars. The Independent Committee is of the opinion that the mistake committed by Individual B and Individual C in respect of the distribution of bonus is unacceptable. The Independent Committee recommends the management of the Company to take appropriate disciplinary actions against the relevant individuals.

2. In respect of any loss which may be suffered by the Company as a result of the 1st Unresolved Issue, the Independent Committee recommends that the Company seeks compensation from the former shareholder of Shanghai Xinla, Individual A. The Independent Committee noted that the former ultimate holding company of Shanghai Xinla, (as a promisor) and the former shareholder of Shanghai Xinla, Individual A (as a guarantor) issued a letter of undertaking to the Company, and undertook that they shall be jointly and severally liable for any financial losses suffered by Shanghai Xinla and/or the Company as a result of the payment of the off-the-account wages and bonus. The Independent Committee recommends the Company to follow-up on this in accordance with the sales and purchase agreement for the acquisition of Shanghai Xinla and the above letter of undertaking.
3. In respect of the internal control issues identified by the Independent Investigator, relevant remedial measures shall be taken in accordance with the recommendations of the Independent Investigator.

The Independent Committee has recommended the Board to endorse the findings of the Independent Investigation and the remedial measures recommended by the Independent Committee.

The Board has considered the findings of the Independent Investigation and the recommendations of the Independent Committee. The Board resolved that it endorses the findings of the Independent Investigation and agrees with the recommendations of the Independent Committee. The Board confirms that the Company has implemented all remedial measures recommended by the Independent Committee.

CONTINUED SUSPENSION OF TRADING

At the request of the Company, trading in the shares of the Company on the Stock Exchange has been suspended with effect from 9:00 a.m. on 31 March 2020 and will continue to be suspended until the Company fulfils the Resumption Guidance.

Shareholders and potential investors are advised to exercise caution when dealing in the shares of the Company.

By order of the Board
7Road Holdings Limited
Meng Shuqi
Chairman

Wuxi, the PRC
3 June 2020

As at the date of this announcement, the executive Directors are Mr. Meng Shuqi, Mr. Li Zhengquan and Mr. Yang Cheng; and the independent non-executive Directors are Mr. Xue Jun, Ms. Li Yiqing and Ms. Wang Ying.