

Stock code: 002032

Short form: Supor

Announcement No.:2021-003

Announcement on Reply to Regulatory Inquiry of Zhejiang Securities Regulatory Bureau

This Company and all members of the Board of Directors hereby warrant that all information disclosed here are true, accurate and complete, and contain no fictitious statement, misleading information or significant omission.

Zhejiang Supor Co., Ltd. (hereinafter referred to as “Company”, “the Company” or “Supor”) received Regulatory Inquiry (ZZJGS ZI [2020] No. 140) issued by Zhejiang Securities Regulatory Bureau (hereinafter referred to as “Inquiry Letter”) on December 28, 2020. The reply on relevant matters regarding the Inquiry Letter of the Company is announced as follows:

- 1. Zhejiang Securities Regulatory Bureau issued a Warning Letter as an administrative regulatory measure to Zhong Shen Zhong Huan Certified Public Accountants (Special General Partnership) and CPAs Li Wei and Li Huihui on problems existing in the auditing process of the financial statements of 2019 fiscal year of Supor. According to the regulatory measure, your company carried out a new business of "advance payment financing" in 2019 and signed a tripartite acceptance agreement with distributor(s) and bank(s) with a total contract amount of 900 million yuan. (I) Please explain in detail the business model of "advance payment financing", the risks assumed by your company and the risk control measures adopted by your company. Please explain the management and control system of distributor(s) signing the said tripartite acceptance agreement, including their qualifications and credit management, etc. (II) Please verify whether each distributor signing the above agreement is related to your company, whether the company's pricing for every such a distributor is fair, whether your company implements "overstock" over them and whether there is profit transfer. The annual audit accountant(s) is hereby required to check and express clear opinions.**

(I) Please explain in detail the business model of "advance payment financing", the risks assumed by your company and the risk control measures adopted by your company. Please

explain the management and control system of distributor(s) signing the said tripartite acceptance agreement, including their qualifications and credit management, etc.

Reply:

1. Business mode

The new business "advance payment financing", namely the tripartite acceptance business, is a financial product launched by banks to solve the "financing difficulty" problem of small and medium-sized enterprises. In 2019, the Company introduced this financial product in order to solve the capital demand problems encountered by 31 high-quality distributors in the operation process and to better develop marketing of the Company. The operation mode of the business is that the bank, the Company and the distributor sign the "cooperation agreement" and "advance payment financing cooperation agreement" respectively. According to the above agreement, the bank issues an electronic acceptance bill for no more than 6 months based on the distributor's fund demand under the condition that all parties' conditions are met,. The acceptance bill is directly paid to the Company for purchasing goods, and is booked in the receivables financing account of the distributor by the Company. If the distributor fails to repay the difference between the cash deposit and the amount of the acceptance bill after the maturity of the acceptance bill, the Company may bear part of the loss of the difference that the distributor has not paid to the bank. But such loss will not exceed the loss of accounts receivable that the distributor has made to the Company without using the "advance payment financing". If such loss occurs without using the "advance payment financing", it will be booked in the accounts receivable of the Company accounts receivable bad debt account. Up to now, all distributors participating in this financial business are in good condition, and there is no case that the Company suffered losses due to overdue repayment of acceptance bills.

2. Potential Risks

The loss of the Company under the "advance payment financing" should be recognized as the bad debt loss of the Company's accounts receivable from distributors; and the Company will not have to bear the guarantee liability loss other than the loss of accounts receivable under this business mode.

3. Risk control measures taken by the Company

In order to strengthen the management of working capital and standardize the release and management of distributors' credit line, the Company has developed Credit Policy Management Rules. These Rules explicitly stipulate the management measures for the "advance payment financing" business, including

prerequisites (entry criteria) for customers to apply for "advance payment financing", credit line evaluation standards, limits for examining and approving authority and follow-up management, etc.

The Company has implemented the corresponding control measures in the process of business development in a rather strict and standardized way. Therefore, the risks in this business is relatively put under control. Up to now, all distributors engaged in this business are in good standing and do not incur any circumstance that any of them fails to repay upon the maturity of the acceptance bill and leads to losses against the Company. The Company will add detailed information disclosure regarding the "advance payment financing" business in periodic reports and perform internal governance approval process based on the estimated amount.

(II) Please verify whether each distributor signing the above agreement is related to your company, whether the company's pricing for every such a distributor is fair, whether your company implements "overstock" over them and whether there is profit transfer. The annual audit accountant(s) is hereby required to check and express clear opinions.

After verification by the Company, all distributors signing the above agreement are not related to the Company. The Company implements a unified pricing system and supplies the same product to all distributors at the same price. Therefore, the Company did not supply the same product to the above distributors at varied prices and nor profit transfer. The Company signs a distribution agreement with all distributors each year and each distributor decides the time and quantity of replenishment of goods at his/her discretion according to the credit limit agreed in the distribution agreement. Therefore, the Company was not engaged in "overstock" over distributors who participated in "advance payment financing" business.

Audit opinions of annual audit accountants

We have implemented the following verification procedures:

(1) We have acquired the relevant information of the Company's related parties by acquiring the list of related parties and management statements provided by the Company, consulting the information of senior management personnel disclosed in the annual reports of the Company in recent years, checking the information of core management personnel disclosed in the stock incentive plans of the Company in recent years, etc.; we also inquired the above-mentioned distributors' business information, and relevant information of the actual controllers, shareholders, management personnel and other related parties of the above-mentioned distributors through public channels such as TianYanCha; we further inquired

relevant information on the investment of the Company's management personnel through public channels; we verified and compared the above information;

(2) We learned key internal controls related to sales pricing and credit management, evaluated the design of these controls, confirmed their implementation, and tested the operational effectiveness of relevant internal controls;

(3) On the basis of learning and controlling examination of the sales mode of the Company's distributors, we conducted random sampling inspections on distributor contracts and compared the terms and conditions of the contract of distributors engaged in the "advance payment financing" with those of other distributors; we randomly checked the sales records of the current period and compared the sale prices and rebates of similar products between distributors engaged in the "advance payment financing" and other distributors;

(4) We compared the sales growth of distributors engaged in the "advance payment financing" in the current period with that of other distributors, and with that of other listed companies in the same industry in the current period; we conducted monthly analysis on the sales of distributors in recent years to verify whether their sales of the current period keeps in line with the seasonal law of the Company's products; we checked the sales return after reporting period of distributors engaged in the "advance payment financing"; we also checked the payment after reporting period of distributors engaged in the "advance payment financing";

(5) We analyzed the changes in the book balance of the accounts receivable (or deposit received) of distributors engaged in the "advance payment financing", checked whether there is any abnormality, and confirmed with distributors by letter.

After verification, we believe that there is no association between distributors engaged in the "advance payment financing" and the Company. The Company has implemented a fair price for them and "overstock" or profit transfer to these distributors are not found.

II. According to the regulatory measure, Zhong Shen Zhong Huan did not implement proper audit procedures over the consignment inventory stored in distributor(s) of your company. Please explain the causes of the said consignment inventory of your company and the specific management and control methods, including but not limited to the storage and counting methods of the consignment inventory, and the reconciliation with distributor(s). Please explain whether the accounting recognition of the said consignment inventory and the amount of its depreciation

reserves are accurate. The annual audit accountant(s) is hereby required to check and express clear opinions.

Reply:

1. Cause of the Company's consignment inventory

Our offline sales channels of CW in domestic market mainly include international stores and domestic stores. Due to the business of some supermarkets is directly operated by the Company itself but lacking of local logistics distribution system in China, the distributors are in the charge of local logistics distribution for such CW products, and the Company shall pay the corresponding distribution fees to them. As a result, the process management need of consignment inventory of CW in distributors is existing.

2. Supervisory and management measures on consignment inventory

In order to strengthen the consignment inventory management of distributors, the Company signed the Agreement for Distributed Product Storage and Warehousing Lease with distributors which clearly regulated the responsibilities and management measures to be undertaken by the distributors for storage, inventory-checking and reconciliation. Meanwhile, the Company has also established corresponding supervisory and management measures on consignment inventory, and clarified the requirements on reconciliation and inventory-checking for consignment inventory to ensure the safety and integrity of consignment inventory in whole process.

3. Accounting recognition of the consignment inventory and its depreciation reserves

(1) Accounting recognition of the consignment inventory

Products shipped by the Company to each inventory consignment warehouse are reckoned as warehouse shifting of inventory in IT system, in specific, the inventory in the consignment warehouse is increased but the inventory in the Company's own warehouse is decreased. Such inventory is still recognized as inventory in accounting treatment and financial statement. The consignment warehouse of the Company arranges delivery according to orders placed by supermarkets, sends the acceptance receipt signed and acknowledged by supermarkets back to the Company, and the Company issues VAT invoices and acknowledges the income after verifying the acceptance receipt with each supermarket, and reduces the consignment inventory at the same time. The Company has effective controls over consignment inventory and the accounting recognition of consignment inventory is accurate.

(2) Depreciation reserves of the consignment inventory

The impairment loss of the consignment inventory is calculated and withdrawn in the same way with other inventory stored in own warehouses according to the Company's inventory depreciation reserve policy. As of the end of 2019, the balance of consignment inventory was CNY73.39 million and the balance of inventory depreciation reserves was CNY6.16 million, representing a withdrawal proportion of 8.40%. The provision ratio for inventory depreciation reserves of the Company's consignment inventory was sufficient and reasonable.

Audit opinions of annual audit accountants

We have implemented the following verification procedures:

(1) We learned the processes and internal control systems related to inventory management, delivery and sales revenue confirmation of consignment inventory, and evaluated the effectiveness of the relevant internal control design and operation;

(2) We got the *Agreement for Distributed Product Storage and Warehousing Lease* signed by the Company and distributors who kept the consignment inventory, and reviewed the terms and conditions of custodial responsibilities and obligations for the consignment inventory; We obtained the *Sales Contract* signed by the Company and supermarkets, and checked the terms and conditions of product delivery, acceptance and settlement of product sales;

(3) We carried out spot checks on statements between the Company and distributors who kept the consignment inventory, as well as original documents related to the sales revenue between the Company and supermarkets, including statements with supermarkets, acceptance confirmation forms issued by supermarkets, supply invoice confirmation forms, etc.;

(4) We conducted inventory monitoring on some consignment inventory warehouses for checking the status of the consignment inventory; we checked the inventory monitoring records with the book records;

(5) We sent letters to distributors who kept the consignment inventory for confirming the accuracy of the ending balance of the consignment inventory; and sent letters to supermarkets for confirming the accuracy of accounts receivable;

(6) We learned the Company's inventory depreciation calculation and withdrawing policy and reviewed the calculation results of inventory depreciation at the end of the year.

After verification, we believe that the accounting confirmation of consignment inventory and the amount of provision for inventory depreciation are accurate.

III. According to the regulatory measure, it is found that there are defects in the internal control

management of Zhong Shen Zhong Huan and that many audit procedures were not properly executed. Please explain your company's arrangement for auditing the 2020 annual report, whether the audit services provided by Zhong Shen Zhong Huan can guarantee the audit quality for your company and whether Zhong Shen Zhong Huan is sufficiently independent and professionally competent. Your company's audit committee and independent directors are hereby required to verify and express their opinions on the above issues.

Reply:

1. Audit work arrangement for 2020 Annual Report

The *Proposal on Continuing to Engage Audit Authority 2020* was reviewed and adopted by the 16th Session of the 6th Board of Directors and the Annual General Meeting of Shareholders for 2019 Fiscal Year, agreeing to continue to engage Zhong Shen Zhong Huan Certified Public Accountants (Special General Partnership) as the Company's financial audit agency.

(1) Adjustment of Supor project team members

All members in audit team for 2020 Annual Report are appointed by Zhong Shen Zhong Huan Wuhan Head Office. The audit team consists of five project partners, project managers, senior auditors and seven audit assistants. The project partners, project managers and senior auditors in the audit team have audit experience in annual reports of listed companies.

(2) The main audit work arrangement for 2020 Annual Report

Preliminary audit of statements from Nov. 9, to Nov. 20, 2020 and learning about the Company's operation, financial status and operating results this year. Learning and testing internal control of the Company from Nov. 30, to Dec. 12, 2020. Supervision of inventory and fixed assets, etc. from Nov. 9, to Dec. 31, 2020. On-site audit from Jan. 11, to Feb. 5, 2021. Draft arrangement, audit report preparation, review within the project team and quality control review from Feb. 20, to Mar. 5, 2021. Soliciting opinions for the audit report, communication with the management and issuing audit report from Mar. 8, to Mar. 31, 2021.

2. Audit independence, qualification and audit quality of Zhong Shen Zhong Huan

(1) Information of Zhong Shen Zhong Huan Certified Public Accountants and Wuhan Head Office

Zhong Shen Zhong Huan Certified Public Accountants (Special General Partnership), formerly known as Wuhan China Certified Public Accountants of the Ministry of Finance established in 1987, is one of the first large accounting firms in China granted the qualification for being engaged in auditing

security, futures and financial business. In November 2013, it was restructured into a special general partnership as required by the Ministry of Finance and other competent authorities of the industry. At present, Zhong Shen Zhong Huan has a total of 1,716 Chinese CPAs, 91 international CPAs, 17 national accounting leaders, 27 provincial accounting leaders and 93 experts from the consulting expert database above the provincial and ministerial level. Wherein: Zhong Shen Zhong Huan Wuhan Head Office, established in 1987, has been granted a business certificate as an accounting firm (certificate No: 42010005) from the Department of Finance of Hubei Province. Wuhan Head Office has been engaging in securities service since it was granted the business license of securities and futures as an accounting firm in 1993. Now, it has 610 employees, including 228 CPAs.

(2) Main clients of Zhong Shen Zhong Huan

Zhong Shen Zhong Huan provides services for 179 A-share listed companies, large state-owned enterprises, 282 large local state-owned enterprises, more than 1,100 foreign-funded enterprises and over 300 NEEQ enterprises in China. Among them, Zhong Shen Zhong Huan provides services for the following A-share listed companies in addition to Supor: Gree Electric Appliances, Xinhuanet.com, AVIC Capital, AVIC Electromechanical, AVICHT, GD Power, HG TECH, Changjiang Securities, Wushang, San'an Optoelectronics, Yunnan Baiyao, C&S Paper Co., Ltd. etc.

(3) Rewards and punishments of Zhong Shen Zhong Huan

In the past 3 years, Zhong Shen Zhong Huan has not been subject to criminal punishment, administrative punishment or disciplinary sanction. As to the 20 warning letters issued by local securities regulatory bureaus of the CSRC as administrative supervisory and administrative measures received in the past 3 years, Zhong Shen Zhong Huan has completed the rectification as required and submitted the rectification report to such bureaus.

(4) Information of Supor's annual report audited by Zhong Shen Zhong Huan

Since Zhong Shen Zhong Huan was employed by the General Meeting of Shareholders of the Company as the annual report audit institution in 2016, it has been adhering to the principle of independent audit in the audit process over the years, objectively and fairly reflected the financial situation of the Company, earnestly performed the obligations of an audit institution, and safeguarded the legitimate rights and interests of the Company and shareholders in a professional way. For the time being, the Company has not found any relationships or matters that may affect the independence in project team members of Zhong Shen Zhong Huan in the process of annual report audit of Supor, or any

violations of the requirements for independence of the *Codes of Professional Ethics for Certified Public Accountants in China*.

3. Rectification plan

It is understood that Zhong Shen Zhong Huan held a special meeting, organized a special team to deploy the rectification and implementation work, and submitted a written rectification report after receiving the Decision on Issuing A Warning Letter to Zhong Shen Zhong Huan Certified Public Accountants (Special General Partnership) and CPAs Li Wei and Li Huihui issued by Zhejiang Securities Regulatory Bureau on November 11, 2020. The rectification scheme focuses on the "quality control and practice quality", including the work assignment, guidance and supervision of the project team, the review of project quality control, the verification of the audit team members, the improvement of working papers, and the enhancement of project supervision.

4. Verification opinions of the Audit Committee and independent directors

The 43rd Audit Committee was held on January 5, 2021, all members of Audit Committee, independent directors, part of top management and accountants from Zhong Shen Zhong Huan attended this meeting in person. This meeting is mainly focus on the questions, that is, whether the audit services provided by Zhong Shen Zhong Huan can guarantee the audit quality for the Company and whether Zhong Shen Zhong Huan is sufficiently independent and professionally competent. All members of Audit Committee and independent directors have reviewed the competence and independence of Zhong Shen Zhong Huan from five aspects including company history and business scope, professionals and integrity record, qualification, competence and independency of audit team members, the corrective actions in correspondent to the regulators' requirements and annual audit plan for 2020 fiscal year, and concluded that after corrective actions were taken Zhong Shen Zhong Huan has valid qualification and necessary competence to ensure the quality of annual audit work of the Company. And also no specific issues were noted to affect the independence of the external auditor. In order to further enhance and ensure the independency and competence of the audit mission, the Audit Committee and independent directors required that in addition to actively and effectively implementing corrective actions, Zhong Shen Zhong Huan should replace at least one of the signing CPAs with more senior and experienced partner. In addition, they further raised two points regarding Zhong Shen Zhong Huan's work: on one hand, on-site working time of signing CPAs should be improved and on the other hand, the issue raised by the regulators should be put emphasis on during the audit work for 2020 annual report.

Board of Directors of Zhejiang Supor Co., Ltd.

January 11, 2021