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AUSNUTRIA DAIRY CORPORATION LTD
澳優乳業股份有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock code: 1717)

SUPPLEMENTAL ANNOUNCEMENT IN RELATION TO THE ANNUAL RESULTS AND THE ANNUAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2022

References are made to the annual results announcement of Ausnutria Dairy Corporation Ltd (the "**Company**", together with its subsidiaries, the "**Group**") for the year ended 31 December 2022 published on 30 March 2023 (the "**2022 Annual Results Announcement**") and the annual report of the Company for the year ended 31 December 2022 published on 26 April 2023 (the "**2022 Annual Report**"). Unless otherwise defined herein, capitalised terms used in this announcement shall have the same meanings as those defined in the 2022 Annual Results Announcement and the 2022 Annual Report.

As disclosed in the 2022 Annual Results Announcement and the 2022 Annual Report, the Company made eight prior year adjustments to its comparative figures for 2021 to correct various prior period accounting errors identified. These errors relate to the accuracy of (i) the recognition for sales incentive program; (ii) trade and bills receivables provision for certain customers; (iii) share of profits and losses of investments accounted for using the equity method; (iv) inventory provision; (v) prepayments, deposits and other assets; (vi) inter-company transactions elimination; (vii) provision for employees with long term sick leave; and (viii) income tax payable. In this connection, the Company would like to supplement the information disclosed in the 2022 Annual Results Announcement and the 2022 Annual Report as follows:

ERROR (I) – THE RECOGNITION FOR SALES INCENTIVE PROGRAM

Circumstances and reasons leading to error (i)

Error (i) relates to overstatement of revenue, selling and distribution expenses and income tax expense in respect of the sales incentive program provided to distributors. As part of the business model of the Group, the Group enters into a large number of sales contracts with distributors in Mainland China, and includes various incentives provided to distributors in the form of volume rebates, discounts and other promotion and marketing supports. The consideration received or receivable from the distributors is allocated between the products immediately sold and the incentives for distributors' future redemption. The amount allocated to the incentives is recorded as a contract liability and deferred until the incentives are redeemed. Such allocation involved management consideration of various forms (e.g. volume rebates, discounts and other promotion and marketing supports) and contract terms (e.g. a large number of distributors that have minimum purchase requirements and other conditions under their respective sale contracts) of the sales incentive program. Determining and quantifying the material amount of contract liabilities involved complex computation and allocation against sales revenue. The calculation of financial impact which reflected as contract liabilities to the Group also involved complicated formulae with application of different parameters.

As the Group experienced prolonged period of growth and financial success for four consecutive years from year 2018 to year 2021, the errors related to the parameters used in the computation of the contract liabilities, which should have been discovered in evaluating the Group's overall profitability, were not identified at the time as the increase in the Group's profitability were in line with the increase in revenue during such period. As a result, the then directors of the Company were of the view that, although they have undertaken all the work necessary to fulfil their fiduciary duties, error (i) was not timely discovered. Further, the Company has engaged its previous auditor to conduct certain procedures regarding the historical quarterly consolidated financial statements of the Company and nothing has been brought to the attention of the Company based on their work conducted.

Identification of error (i)

In accordance with the relevant Corporate Governance Code, the Company has been supplying the Board with monthly management accounts and management updates in respect of the Group's financial performance and operations. In their review of the Company's management accounts for the three months ended 31 March 2022, the Board noted that the Group's performance declined in terms of both revenue and profits due to the deterioration of market sentiment. Furthermore, the non-executive Directors (who were appointed in March and April 2022) and the new chairman of the Audit Committee (who was appointed in April 2022) noted that there was a significant decrease in the Group's profitability as compared to that for the prior periods which contradicted with the Board's expectation and prompted further investigation. Accordingly, the Board commissioned the Group's management in reviewing the matter in greater details. The management then conducted the review with focuses on the formulae, parameters and mathematical accuracy of the historical calculation model of contract liabilities. Certain errors related to the parameters used in the computation of the contract liabilities were identified during the review which led to the discovery of error (i) and relevant adjustments were made in this regard in the interim financial statements of the Company for the six months ended 30 June 2022.

After the publication of the interim results announcement and interim report of the Company for the six months ended 30 June 2022, the Board observed that significant fluctuation in profitability still existed. Having considered that the accounting treatment for the sales incentive program involved significant data and complex computation and was not a straight-forward issue that the Board may easily identify, the Board further commissioned the Group's management in conducting a comprehensive review related to sales incentive program including the review of underlying data and balance points owed to all distributors in operation systems. Together with the technical supports on financial reporting provided by the Company's current controlling shareholder which possesses unrivalled industry experience and expertise in the PRC dairy industry, the Company identified further discrepancies in respect of the sale incentive program by themselves.

In order to ensure that the adjustments in connection with error (i) have been properly made, the Company has (i) compared the adopted accounting treatment with the relevant accounting standards and did not notice any material discrepancy and (ii) revisited the sales incentive program calculation sheets and updated the calculation including:

(a) extracting the sales incentive records from the operation system;

(b) comparing the operation system data with the distributor confirmations;

(c) reviewing and updating the key assumption for sales incentive estimation by comparing with contract terms, and historical/subsequent settlement;

(d) verifying the working paper of accrued expenses and comparing the source data with contract liabilities to identify any overlap;

(e) checking the reasonableness of the formulae used and mathematical accuracy in conformity with International Financial Reporting Standards 15; and

(f) recalculating the contract liabilities balances based on the updated sales incentive records stated above.

As such, other than error (i), the Company did not notice any other irregularities in the accounting for sales incentive program in previous years. In addition, the Company has discussed the aforementioned review and actions conducted with PricewaterhouseCoopers ("**PwC**"), the current auditor of the Company, and provided PwC with the corresponding documents.

The management of the Company has also conducted internal review on error (i) during the preparation of its consolidated financial statements for the Year 2022 and kept communications with the Audit Committee by reporting the results of the internal review including the circumstances and reasons leading to error (i) and how to evaluate and achieve the accurate amount of error (i).

The Board further commissioned the Group's management to amend the relevant disclosures in the 2022 Annual Report (including disclosures relating to the financial impact of error (i) for each of the past five financial years immediately preceding the Year 2022 as set out on page 172 of the 2022 Annual Report).

Audit Committee's and Auditors' views on error (i)

Based on the audit conducted by PwC in accordance with Hong Kong Standards on Auditing issued by Hong Kong Institute of Certified Public Accountant and the audit evidence obtained, PwC has issued its unmodified audit opinion for the consolidated financial statements of the Group for Year 2022, as a whole, which is presented on pages 61 to 65 of the 2022 Annual Report under the section headed "Independent Auditor's Report".

The Audit Committee communicated with PwC in relation to its audit procedures performed and the results of the procedures related to error (i) during its audit of the consolidated financial statements for the Year 2022. Based on the work performed and the communications conducted above, the Audit Committee evaluated the nature of error (i), the adequacy and appropriateness of the work performed by management and understood the work performed by PwC. The Audit Committee concluded that it is satisfied that the adjustments made in relation to error (i) have been properly made and addressed all material misstatements in previous years.

ERRORS (II) TO (VIII)

Circumstances and reasons

Set out below is a table summarising the circumstances and reasons for each of error (ii) to error (viii):

Errors	Circumstances and reasons
Error (ii) – trade and bills receivables provision for certain customers	Error (ii) relates to understatement in provisions for account receivables, which was resulted from a credit loss of accounts receivables of a customer in the Group's operations in the Netherlands.
Error (iii) – share of profits and losses of investments accounted for using the equity method	Error (iii) relates to an understatement in the share of losses of an associate in the Netherlands.
Error (iv) – inventory provision	Error (iv) relates to an understatement of inventory provision and cost of sales, which was resulted from the loss of certain slow moving finished goods of the Group.
Error (v) – prepayments, deposits and other assets	Error (v) relates to an overstatement of long-term prepayments and deposits, with inappropriate calculation.
Error (vi) – inter-company transactions elimination	Error (vi) relates to an error in eliminating the inter-company transactions took place during 2021, which caused part of the unrealized profits not been eliminated as a result.
Error (vii) – provision for employees with long term sick leave	Error (vii) relates to an under-provision of leave pay accruals for employees with long term sick leave in the Netherlands by 2021.
Error (viii) – income tax payable	Error (viii) resulted in an understatement in tax expenses in year 2021, and understatement of income tax payable and deferred tax assets as at 31 December 2021, and understatement of income tax payable as at 1 January 2021, mainly due to the historical periods discrepancy of income tax liability compared with the actual annual tax return from the tax authority.

Identification of errors (ii) to (viii)

Errors (ii) to (v) were discovered during the preparation for the Company's consolidated financial statements for 2021 and in the course of 2021 year-end audit. These errors were considered individually and in aggregate immaterial in nature and amount at the time of issuing the Company's annual report for 2021.

Having considered the quantitative and qualitative factors, the Company, after consulting with previous auditors, determined the amounts were immaterial at the time when compared with the overall effect on the financial statements and decided not to take up the adjustments in connection with errors (ii) to (v) in the Company's consolidated financial statements for 2021.

Errors (vi) to (viii) were discovered during the preparation of the consolidated financial statements for the Year 2022 and in the course of year-end audit (i.e. during the first quarter of the year ending 31 December 2023), when an in-depth review of the Group's financial information for 2021 and 2022 was carried out following the discovery of error (i). Nevertheless, the Company was of the view that the adjustment amounts for errors (vi) to (viii) were individually immaterial.

However, the Company decided to correct all the aforementioned errors taking into consideration the accumulated impact and for better corporate governance consideration in the 2022 Annual Results Announcement and the 2022 Annual Report.

In order to ensure that the adjustments in connection with error (ii) to (viii) have been properly made, the Company has compared the adopted accounting treatment with the relevant accounting standards and did not notice any material discrepancy. In addition, the management of the Company has further undertaken the following actions:

Errors	**Actions conducted by the Company**
Error (ii) – trade and bills receivables provision for certain customers	In 2022, the Company has reviewed the financial position of the customer and communicated with the customer, based on which the Company finalised the amount of expected credit loss. Meanwhile, the Company revisited the trade receivables aging report as at 31 December 2021 and reviewed the subsequent collection of trade receivables in 2022. As such, other than error (ii), the Company did not notice any other irregularities in the accounting for expected credit loss in the prior year financial statements.
Error (iii) – share of profits and losses of investments accounted for using the equity method	The Company obtained and reviewed the audited financial statements as at 31 December 2021 of investees accounted for using the equity method, and compared the audited financial figures with the management accounts which was used for equity method accounting treatment and performed the recalculation based on the audited financial statements. As such, other than error (iii), the Company did not notice any other irregularities in the accounting for investments accounted for using the equity method in the prior year financial statements.
Error (iv) – inventory provision	The Company revisited the inventories list as at 31 December 2021 to identify any material inventories close to the expiration dates which indicated the net book value of inventories might be lower than the net realisable value. In addition, the Company reviewed the inventories' write off and subsequent sales in 2022. As such, other than error (iv), the Company did not notice any other irregularities in the accounting for inventory provision in the prior year financial statements.
Error (v) – prepayments, deposits and other assets	The Company revisited the contract terms of such prepayments and deposits, and reviewed the updated rate, comparing with the market rate in 2021 as well as the review of the updated calculation sheet. As such, other than error (v), the Company did not notice any other irregularities in the accounting for time value of prepayment in the prior year financial statements.
Error (vi) – inter-company transactions elimination	The Company has revisited the inter-company transaction elimination working paper and reviewed the inter-company transactions, unrealized profit rates and other key assumptions to ensure accuracy and completeness. As such, other than error (vi), the Company did not notice any other irregularities in the accounting for inter-company transaction elimination in the prior year financial statements.

Errors	Actions conducted by the Company
Error (vii) – provision for employees with long term sick leave	The Company has revisited the long-term sick employee list and discussed internally with human resources department to ensure accuracy and completeness. Based on the discussion and review, the Company has updated estimation about the long-term sick leave period to be taken by the sick employees and the salaries to be paid. As such, other than error (vii), the Company did not notice any other irregularities in the accounting for employee benefits in the prior year financial statements.
Error (viii) – income tax payable	The Company has revisited the prior year tax return results, analysed the differences between the accounting book and the tax return by comparing with the tax regulations and requirements. The Company updated the calculation of income tax payable and deferred tax in the prior year financial statements. As such, other than error (viii), the Company did not notice any other irregularities in the accounting for income tax payable in the prior year financial statements.

Audit Committee's and Auditors' views on errors (ii) to (viii)

Based on the audit conducted by PwC in accordance with Hong Kong Standards on Auditing issued by Hong Kong Institute of Certified Public Accountant and the audit evidence obtained, PwC has issued its unmodified audit opinion for the consolidated financial statements of the Group for the Year 2022, as a whole, on 30 March 2023, which is presented on pages 61 to 65 of the 2022 Annual Report under the section headed "Independent Auditor's Report".

The Audit Committee communicated with PwC in relation to its audit procedures performed and the results of the procedures related to the correction of error (ii) to (viii) by management during its audit of the consolidated financial statements for the Year 2022. Based on the work performed and the corresponding documents provided to PwC, including communications among the management, previous auditors, and the Audit Committee during the audit of the 2021 consolidated financial statements, the Audit Committee evaluated the nature of errors (ii) to (viii), the adequacy and appropriateness of the work performed by management and understood the work performed by PwC. The Audit Committee concluded that it is satisfied that the adjustments in relation to errors (ii) to (viii) have been properly made and addressed all material misstatements in the prior year financial statements.

INTERNAL CONTROL REVIEW

As at the date of this announcement, the Company has engaged an external internal control consultant (the "**IC Consultant**") for an internal control review (the "**Internal Control Review**") for the purpose of improving its internal control and financial reporting system.

The IC Consultant's review will be conducted by evaluating the entity's internal control components, design and implementation of controls and performing the test if necessary. The Internal Control Review commenced in June 2023 and will take at least two to three months to complete, subject to the actual progress of the review. The scope of work covers but is not limited to the business cycle of entity level controls, sales and revenue, inventory, and management review procedure on the financial reporting system. The scope of the Internal Control Review may be revisited during the review process.

The Company will make further announcement(s) to update its shareholders and potential investors on the results of the Internal Control Review as and when appropriate.

By order of the Board
Ausnutria Dairy Corporation Ltd
Yan Weibin
Chairman

The PRC, 7 July 2023

As at the date of this announcement, the Board comprises three executive Directors, namely Mr. Yan Weibin (Chairman and Chief Executive Officer), Mr. Bartle van der Meer and Ms. Ng Siu Hung; three non-executive Directors, namely Mr. Sun Donghong (Vice-Chairman), Mr. Zhang Zhanqiang and Mr. Zhang Lingqi; and three independent non-executive Directors, namely Mr. Ma Ji, Mr. Song Kungang and Mr. Aidan Maurice Coleman.