

January 17, 2019

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January 17, 2019
Fanhua (FANH) China

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Fanhua (FANH)

Price	\$ 23.11
Market Cap (USD)	1,502.00 mln
Shares Out	65 mln
S/I	2.5 mln

Fanhua (FANH)

Who Owns Fanhua? Not the U.S. Shareholders

- **In a major restructuring last year**, Fanhua claimed to have sold its P&C division. Actually, the company simply robbed public shareholders. It gave 11 of the 19 companies targeted for sale to a Fanhua executive and misreported the transfers as a sale to a third party. The remaining companies are either mere shells or were transferred to a company we suspect is related to Fanhua executives.
- **We estimate that Fanhua moved** at least \$136 mln in 2017 revenues off the books but still under executive control.
- **In its life as a public company**, Fanhua has regularly enriched its executives by buying companies from individual managers then divesting them again or simply gifting companies to managers, all without disclosure. In our report, we detail more than a dozen such cases, but there are many more.
- **A new share compensation scheme**, the 521 Scheme, has been used to justify paying \$250 mln to company co-founder Lai Qiuping. We believe the plan is simply a diversion. It closely resembles the scheme that collapsed the company's share price in late 2010.¹
- **Our interviews in China** indicate that Fanhua has guaranteed around ¥1 bln in financial products sold by Lai's privately owned company. We believe these are undisclosed related-party transactions.

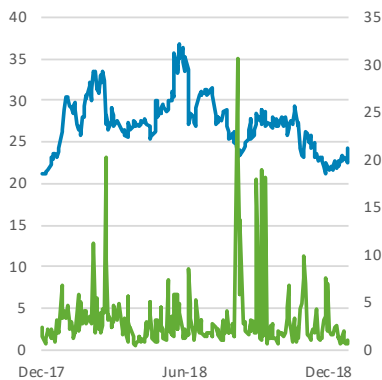
¹ Note: In this report, we use the Chinese format for names, in which the surname comes first. Fanhua disclosures may put the given name first, so Peng Ge in Fanhua disclosures is Ge Peng in our report. We do this to make it easier for third parties to check our information, because we make clear which portion of the name is the surname.

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Fanhua (FANH) last share price in USD (left, blue) and volume in 100k shares (right, green)



Source: Bloomberg January 15, 2019

- ▶ **Fanhua developed** a huge commercial real estate project in the founder's hometown for more than two years without telling investors. Fanhua has been pre-selling residential units there for delivery in 2020—which puts the company on the hook to spend to build out those units. The project was finally mentioned, in passing, on a November 2018 company conference call.
- ▶ **Investors are skeptical** that regulators are doing their job in China—how much of this company's value has been stolen? Based on the evidence, we believe this company is uninvestable.

January 17, 2019

Table of Contents

Who Owns Fanhua?	<u>1</u>
Executive Summary	<u>5</u>
The sale that wasn't	<u>5</u>
Yang Lin: a proxy for Fanhua management	<u>11</u>
Looking for Yang Lin's companies	<u>12</u>
"I don't know anything about a sale"	<u>16</u>
Is Cheche a proxy for Fanhua insiders?	<u>16</u>
Not the first fake transaction	<u>19</u>
Round trip	<u>20</u>
Lining the Founder's Pockets	<u>23</u>
Déjà vu all over again	<u>26</u>
Enriching insiders, stiffing shareholders	<u>29</u>
Undisclosed guarantees	<u>36</u>
Fanhua's secret real estate development	<u>38</u>
Sell	<u>39</u>
Appendices	<u>40</u>
Disclaimer	<u>50</u>

January 17, 2019

Executive Summary

Fanhua (FANH) is a U.S.-listed, China-based company that claims primarily to distribute insurance products. Before Q4 2017, most FANH income came from property and casualty insurance. In Q4, the company claimed to divest most of its P&C insurance business, as well as its insurance brokerage business. Currently, the company is described in its disclosures as primarily a distributor of life insurance.

Over the course of our months-long investigation of FANH, we concluded that Fanhua Inc. is nothing but a shell game among related parties that allows executives to loot investor cash. We detail how the executives running Fanhua have made undisclosed payments and loans to insiders, used “share incentive plans” to hand themselves cash, and covertly transferred equity in subsidiaries to ensure that investor cash goes into executive pockets.

Most recently, executives stole a big chunk of the insurance business right from under investors’ noses, purloining companies that they had reported sold to a third party. We examined the financial statements of all 19 companies Fanhua supposedly sold to a company called Beijing Cheche. Not only were most companies NOT sold to Cheche, but the biggest portion of revenue was given to a Fanhua executive.

The Cheche transaction was just one in a series of Fanhua deals that are not what they appear to be. Fanhua has regularly acquired shell companies belonging to undisclosed insiders. It has given away equity without disclosure. Our checks of public records show that Fanhua shareholders are not the owners of around half of the companies listed on Fanhua’s official website.²

The sale that wasn’t

On October 27, 2017, Fanhua announced that it would sell its P&C insurance division for ¥220 mln, or \$31.8 mln. The company said the buyer, Beijing Cheche Technology, would pay \$13.7 mln in cash and the balance in a note payable over three years with 8% interest.³ Based on the financial statements of the target companies and on comparables, we calculate that this price is equivalent to 1x P/E.

The transaction was a fake. Fanhua gave Cheche only six of the 19 target

² See appendices for brief descriptions of [key executives](#) and [companies](#).

³ Should Cheche fail to pay the second part of the consideration—which appears to be contingent upon achieving a certain revenue target—then the loan will convert back to Fanhua equity.

January 17, 2019

companies it listed in a sales contract attached to its 2017 20-F. Furthermore, we suspect that Cheche itself may be an undisclosed related party.

Eleven of the companies were given to a Fanhua executive. Of the remaining two, one appears not to exist, and the other has been shifted to joint ownership by Fanhua and the “buyer.”

We visited the head office of the company that now owns most of Fanhua’s P&C businesses, supposedly sold to Beijing Cheche. That office is pictured below.



Photo by J Capital, November 2, 2018

The share purchase agreement filed by Fanhua describes Cheche as a “third party” that “operates an online auto insurance platform.”

SHARE PURCHASE AGREEMENT

dated as of

September 2017

in

Beijing

Among

BEIJING CHECHE TECHNOLOGY CO., LTD.

FANHUA INSURANCE SALES SERVICE GROUP COMPANY LIMITED

and

FANHUA TIMES INSURANCE SALES & SERVICE CO., LTD.

Screenshot: first page of Exhibit 4.9, Fanhua 20-F filed April 20, 2018

January 17, 2019

Fanhua claimed that it was selling the 19 target companies in order to focus on higher-margin life insurance sales. But this too was a lie. Fanhua continues to sell P&C, and the offloaded companies also sell life insurance. Nor can this be regarded as transitional: the transaction was completed more than a year ago, but when we called the 19 companies that Cheche “bought,” most said they still sold life insurance. One said that the majority of sales comes from life insurance.⁴ These facts further show the breadth of the fraud.

In fact, Fanhua’s own website supports our conclusion that the company lied about the sale, using it as cover to transfer prime assets to Fanhua management at a bargain price. [The Fanhua Holdings website](#) should represent companies owned by FANH, and yet several of the companies listed in the 2017 20-F as part of the sale to Beijing Cheche Technology are still on Fanhua’s website as the advertised agents for life insurance. For example, Dongguan Nanfeng Jiayu was listed on the Fanhua Holdings website as of November 24, 2018 as the company handling life insurance sales for Dongguan, Guangdong. Fanhua reported that it sold that same company as part of the effort to offload P&C insurance sales.



Screen capture from Fanhua Inc. (<http://www.fanhuaholdings.com/gvfh/fhjg/index.shtml>)

Theoretically, the Fanhua China website should now show companies that exclusively sell life insurance. Several of the companies on the website post their revenues from life vs P&C insurance, but only one has a high proportion of life insurance sales. Shandong Fanhua Times reported ¥330 mln in life insurance sales in January through August 2017 and ¥230 mln in P&C sales. Ironically, Shandong Times was among the companies supposedly sold to Cheche.

⁴ See interviews in Appendix B

January 17, 2019

“Our company is still Fanhua. There has been no acquisition, just a shift in selling auto insurance.”

A representative of one of the target companies supposedly sold to Cheche told us over the phone: (our translation) "I figure Cheche just wanted to use Fanhua's license to sell auto insurance. Our company is still Fanhua. There has been no acquisition, just a shift in selling auto insurance."

Even more stunning, employees we spoke with at nine of the target companies supposedly sold to Cheche do not know they were sold. Two more of the target companies appear not to exist, and an employee at yet another told us the company has not been in the insurance business for a decade. Employees we reached at several of the companies had never even heard of the purported acquirer, Beijing Cheche. Others of the target companies emphatically confirmed that their companies had not been sold and continued to belong to Fanhua. One of the companies told us that it was soon to become “a direct subsidiary of Fanhua.” Another, said, "Actually, we are the Fanhua sales team." ⁵

In the sale, Fanhua said it valued the companies at ¥130 mln (\$18.8 mln) more than their net asset value. We do not consider asset value relevant to a sales agency. Fanhua also said the divested companies would achieve a minimum of ¥2 bln--\$287 mln—per year in revenue in each of the next three years. The wording is as follows:

The Target Company is an insurance agency specializing in the distribution of automobile insurance products and in good standing, with the capacity of achieving no less than RMB2 billion auto insurance premiums each year from 2018 to 2020.

We looked at the financial statements of a competitor to Fanhua in China, also an insurance sales agent, called Datong. That company has a net margin of 11%. If the companies that Fanhua divested earned 11% on ¥2 bln in revenue, they would make \$31.4 mln per year in profit. In that case, the total consideration of \$31.8 mln would represent approximately one year of company profit—a P/E ratio of 1x. Payment, furthermore, per the terms of the agreement will be received in three years at best.

Clearly, there is something wrong.

We obtained 2016-2017 financial statements for all the companies on the Fanhua Target List, which can be found on Schedule 1, page 9 of Fanhua's 2017 20-F and in Appendix A to this report. Ostensibly, the sale was to

⁵ Interviews in Appendix B. Interviews have been anonymized to protect employees who spoke with us

January 17, 2019

Cheche. In reality, a shell company owned by a Fanhua executive got 11 of the 19 companies. The total revenue for those companies greatly exceeded the revenue for the few companies that were transferred to Cheche.

Chart 1. Summary of 2016-2017 Revenue of 19 Target Companies Reportedly Sold to Cheche⁶

Target Company	2018 Ownership	2017 Revenue (USD)	2016 Revenue (USD)
Beijing Fanlian Insurance Agency Co., Ltd.	Cheche	\$0	\$0
Beijing Fanhua Insurance Agency Co., Ltd.	Cheche	\$0	\$0
Beijing Fanhua Fumin Insurance Agency Co., Ltd.	Cheche		\$0
Tianjin Fanhua Xianghe Insurance Agency Co., Ltd.	Fanhua Executive	\$452,203	\$281,091
Hebei Fanlian Insurance Agency Co., Ltd.	Fanhua Executive	\$1,153,855	\$3,777,819
Shenyang Fangda Insurance Agency Co., Ltd.	Fanhua Executive	\$700,975	\$1,502,540
Nanjing Yukai Insurance Agency Co., Lt	Fanhua Executive	\$339,067	\$1,222,493
Hangzhou Fanhua Zhixin Insurance Agency Co., Ltd.	Cheche	\$1,697,107	\$2,681,353
Ninbo Baolian Insurance Agency Co., Ltd.	Fanhua Executive	\$11,623,598	\$11,006,454
Jiaxing Lianbao Insurance Agency Co., Ltd.	70% held by Cheche and 30% by CNInsure Holdings.	\$1,337,356	\$4,327,405
Wenzhou Baolian Insurance Agency Co., Ltd.	Company does not exist	\$0	\$0
Henan Fanhua Anlian Insurance Agency Co., Ltd.	Fanhua Executive	\$14,150,565	\$33,235,907
Changsha Lianyi Insurance Agency Co., Ltd.	Cheche	\$5,078,957	\$8,036,696
Guangdong Nanfeng Insurance Agency Co., Ltd.	Fanhua Executive	\$16,793,925	\$18,394,189
Guangzhou Fanhua Yi'an Insurance Agency Co., Ltd.	Fanhua Executive	\$2,260,654	\$2,471,875
Dongguan Nanfeng Jiayu Insurance Agency Co., Ltd.	Fanhua Executive	\$17,245,391	\$20,716,842

⁶ Using the RMB/USD exchange rate posted at the end of the year.

January 17, 2019

Target Company	2018 Ownership	2017 Revenue (USD)	2016 Revenue (USD)
Foshan Tuohua Insurance Agency Co., Ltd.	Cheche	\$5,223,982	\$5,878,843
Jiangmen Fanhua Zhicheng Insurance Agency Co., Ltd.	Fanhua Executive	\$742,755	\$978,090
Fanhua Kafusi Insurance Brokerage Co., Ltd.	Fanhua Executive	\$11,556,292	\$31,021,550
Total revenue of companies transferred to a Fanhua executive		\$95,007,427	\$124,608,850
Total of companies sold to Cheche		\$12,000,046	\$16,596,892
Total other companies		\$1,337,356	\$4,327,405
Total		\$108,344,829	\$145,533,147

Source: Chinese tax bureaus

The recipient of the 11 target companies is an executive named Yang Lin via his shell company called Sichuan Boxin Xinrui Network Technology.⁷ The “headquarters” of Sichuan Boxin Xinrui’s parent company, called Beijing Boxin Lintong, is pictured on page 6.

It is unclear whether Yang Lin’s Sichuan Boxin Xinrui actually paid anything for the new subsidiaries. Neither Sichuan Boxin Xinrui nor its Beijing-based parent company reported any revenue in 2016 or 2017, and the companies’ registered capital was insufficient to pay the purchase price. Instead, it appears that Fanhua simply gifted its own executive \$95 mln in 2017 revenue in just one transaction that it told investors was a sale to a third party. Adding the other companies given to Yang Lin in 2017-18, Fanhua gave away at least \$135.9 mln in revenue to Yang Lin in 12 months.

A longtime executive of Cheche told us in an interview, “Cheche acquired a portion of Fanhua’s auto insurance, and Yang Lin also acquired some of the companies under Fanhua Times Sales and Service. Currently, those companies are owned by Sichuan Boxin Xinrui Network Technology.”

⁷ See Appendix A. The companies that were transferred to Boxin Xinrui are marked in column 3.

January 17, 2019

Yang Lin: a proxy for Fanhua management

So, who is Yang Lin? Not only did he get companies from the Cheche transaction, but Fanhua handed him several other companies, with total 2017 revenue of \$135.9 mln.

Yang Lin is a longtime senior employee of Fanhua and is reportedly “very close” to Fanhua’s CEO. He may be acting as a proxy for the founders. He maintains a very low profile, but a government official we spoke with in Sichuan Province told us that companies Yang Lin registered there were registered by a “representative of [Fanhua founder] Hu Yinan.”

A July 2017 [article](#) that appeared in a Chinese publication called East Money described Yang as an executive who joined the Fanhua team in 2007. The article praises Yang Lin as the genius behind Fanhua’s success in the Sichuan region called Neijiang. Titled “Fanhua in Neijing: A Beautiful Two-Year Turnaround,” the first paragraph mentioning Yang Lin, from the article pictured below, reads as follows:

Starting August 1, 2015, Yang Lin, the new head of [Fanhua’s Sichuan] Neijiang platform, took office. From the construction of the platform to the development of the organization, in just over a year, the Neijiang platform fully covered three outlying counties and established not only the headquarters in Neijiang City but sales offices in Zizhong, Longchang, and Weiyuan. In August 2015, there were only about 20 employees in Fanhua’s Neijiang area. In just two years, that number grew to 1,626 people.

近机构主力持仓

排名	机构名称	持仓数量 (万股)	持仓市值 (万元)
NO.1	中信证券股份有限公司	1,111.11	1,111.11
NO.2	招商证券股份有限公司	1,111.11	1,111.11
NO.3	中国银河证券股份有限公司	1,111.11	1,111.11

2018-12-17 新大洲A 10.03% 涨停时间 09:49 涨停价 14.42

January 17, 2019

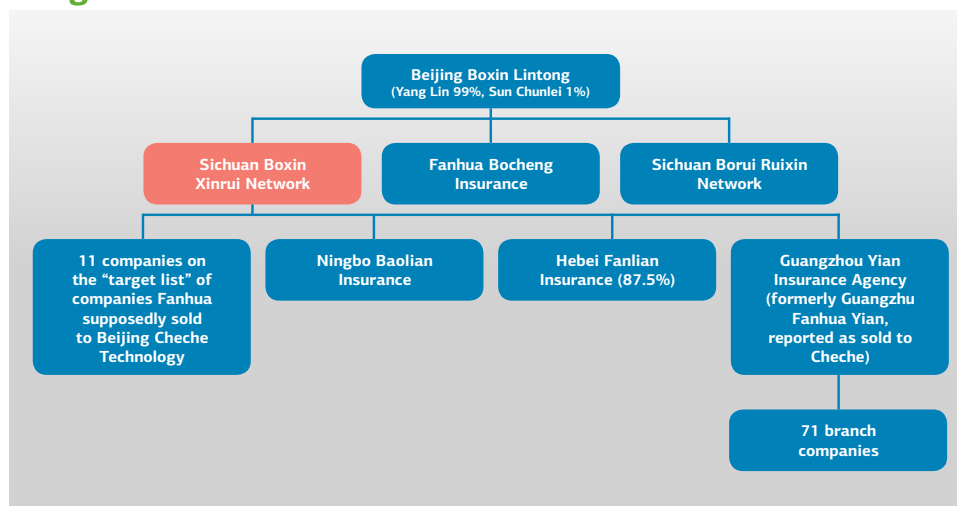
The government record below shows that Yang Lin is “responsible person” of Fanhua Insurance Sales, Sichuan, Neijing Branch.



Record from the Chinese State Administration of Industry and Commerce, J Capital notations

Our interviews with Fanhua employees confirmed that Yang Lin is a Fanhua executive “very close” to Fanhua CFO Ge Peng.⁸

Chart 2. Simplified Diagram of Companies Owned by Yang Lin



Source: Chinese State Administration of Industry and Commerce and J Capital

Looking for Yang Lin's companies

The company that acquired Fanhua subsidiaries in the Cheche transaction is called Sichuan Boxin Xinrui. Official documents for this company indicate that it is headquartered in Sichuan, in the county of Renshou, which

⁸ Chinese government records additionally indicate that Yang Lin is responsible person of five Fanhua companies and shareholder of six that have been gifted assets by Fanhua.

January 17, 2019

is the hometown of Fanhua founder Hu Yinan. We went to Sichuan to find Yang Lin's company.

We looked and looked for Sichuan Boxin Xinrui in the industrial park where it has its official address, but we could not find it. The majority of companies in the park appeared to be making and selling furniture.



This is Boxin Xinrui's registered location in the Xingsheng Industrial Park in Renshou. The registration record does not provide a more detailed address. | Photo by J Capital October 27, 2018

Company name: Sichuan Boxin Xinrui Network Technology Co. Ltd.

Government registration record for Boxin Xinrui

企业名称:	四川博鑫新瑞网络科技有限公司			Date of founding: April 13, 2016
工商注册号:	511421000063693	统一社会信用代码:	91511421MA62J3GX38	Operating condition: in operation
法定代表人:	袁金华	组织机构代码:	MA62J3GX3	
企业类型:	有限责任公司(自然人投资或控股)	成立日期:	2016-04-13	
注册资本:	500万人民币	经营状态:	存续(在贵、开业、在册)	
注册地址:	仁寿县兴盛镇舒坪社区(兴盛家私产业园)			

Registered address: Xingsheng Furniture Industrial Park, Shuping Area, Xingsheng Town, Renshou County

SAIC registration record for Boxin Xinrui. Notations by J Capital

We believe Sichuan Boxin Xinrui is a shell company, with no operations. The company reported zero revenues to its local tax bureau. The registration record pictured above indicates that Sichuan Boxin Xinrui was capital-

January 17, 2019

ized in April 2016 with \$728,000. Its parent company is capitalized at the same level and also has no revenue. It is very unlikely that this company could have paid \$31.8 mln for the Cheche companies a mere 18 months after it was formed.

We went to the local government office in charge of the park to make sure we hadn't missed anything. Officials in the office said there was no Sichuan Boxin Xinrui in the area. Yet we know from Chinese government records that Yang Lin established not only this but four other companies in that industrial park. SAIC records show that four of the five were established on the same day, April 13, 2016 and a fifth later on. We could find no traces of any of the five. That suggests to us that Yang Lin and Fanhua wanted shell companies in an accommodating jurisdiction that would not require them actually to maintain premises or pay taxes.

A longtime government official working in the office park in Renshou, Sichuan remembered the registration. He told us that the companies registered to Yang Lin had been established by "a representative of Hu Yinan." This supports our suspicion that Yang Lin is a proxy for senior management.



Outside government offices in Renshou. | Photo by J Capital October 27, 2018

We checked other locations in the industrial park in case Boxin Xinrui had moved. No one in the area had heard of the company.

January 17, 2019



The companies in the park where Boxin Xinrui has its registered address are furniture companies. | Photo by J Capital October 27, 2018

Sichuan Boxin Xinrui has a parent company, in Beijing, called Beijing Boxin Lintong. Here is the company's government registration record:

企业名称:

北京博信林通科技有限公司

Beijing Boxin Lintong Science and Technology Co. Ltd.

工商注册号:

91110108MA0179GH7L

统一社会信用代码: 91110108MA0179GH7L

法定代表人:

林林

组织机构代码: MA0179GH7

企业类型:

有限责任公司(自然人投资或控股)

成立日期: 2017-09-01

注册资本:

100 万人民币

经营状态: 开业

注册地址:

北京市海淀区永定路2号院4号楼8层一室230号

营业期限:

自 2017-09-01 至 2047-09-01

经营范围:

技术开发; 技术推广; 技术转让; 技术咨询; 销售自行开发的产品; 计算机系统服务; 基础软件服务; 应用软件服务; 软件开发; 软件咨询; (企业依法自主选择经营项目, 开展经营活动; 依法须经批准的项目, 经相关部门批准后依批准的内容开展经营活动; 不得从事国家限制类项目的经营活动。)

Company external investments

Sichuan Boxin Xinrui Network Technology Co. Ltd.

Ownership: 100%

三、企业对外投资

序号	企业名称	营业执照	企业类型	企业状态	注册资本 (万元)	出资比例	法定代表人
1	北京博信林通科技有限公司	91110108MA0179GH7L	有限责任公司	开业	1000	100%	林林
2	四川博信林通网络科技有限公司	91510108MA0179GH7L	有限责任公司 (自然人投资或控股)	存续 (在营、开业、在册)	100	100%	林林
3	四川博信林通网络科技有限公司	91510108MA0179GH7L	有限责任公司 (自然人投资或控股)	存续 (在营、开业、在册)	100	100%	林林

Like Sichuan Boxin Xinrui, Beijing Boxin Lintong reported no revenue and no employees in 2017. Like its subsidiary, registered capital is \$728,000, not enough to pay for the companies acquired by its subsidiary. We visited Beijing Boxin Lintong's registered address, but, like its Sichuanese subsidiary, Beijing Boxin Lintong had no operations. Staff and neighbors in the office park in Beijing said no such company had ever operated at the premises.

January 17, 2019

Yang Lin

二、股东及出资信息 Shareholding and Equity Contribution Information

序号	股东	认缴出资额 (万元)	币种	出资比例	认缴出资日期	国别/地区
1	杨林	99.000000	人民币元	99.00%		
2	孙春磊	1.000000	人民币元	1.00%		

Proportion of Paid-in Capital

Documents showing Beijing Boxin Lintong's ownership of Sichuan Boxin Xinrui and Yang Lin's ownership (99%) of Beijing Lintong. Source: China SAIC via Qixin

"I don't know anything about a sale"

To understand the Cheche sales transaction, we telephoned all 19 companies listed in the Fanhua 2017 20-F "target list" appended to the contract with Beijing Cheche.

Four of the companies could not be found or had all numbers disconnected. One company told us "Actually, we are Fanhua." Another said that they were not supposed to talk about the transaction to outsiders. "There has been no acquisition, just a shift in selling auto insurance," said another. (See Appendix B for detail)

Is Cheche related to Fanhua?

Just a handful of the target companies went to the designated buyer, Cheche, whose name literally means "Car Car." So, who or what is Cheche?

We believe that Cheche may not be quite as arm's-length a buyer as advertised; in fact, it could be an undisclosed related party. We found that one of the owners of Cheche, called Shenzhen Ruiyuan Investment Company (Limited Partnership), was registered at the same Shenzhen address at approximately the same time as Fanhua subsidiary Qunabao and Fanhua co-founder Lai Qiuping's investment vehicle Chengchuang (Shenzhen) Investment Co. Ltd. This supports our view that Cheche could be related to Fanhua. The shared location is not itself proof of a connection; the address accommodates hundreds of companies. But the investor behind Ruiyuan had previously invested in Cheche then pulled out and formed Ruiyuan for the sole purpose of re-investing in Cheche.⁹

⁹ The Ruiyuan founder, Xiong Dan, invested in Cheche in December 2014. He sold his shares a few months later. Right after selling his shares, on June 18, 2015, Xiong Dan established a partnership called Shenzhen Ruiyuan, and Shenzhen Ruiyuan invested in Cheche on July 24, 2015, one month after the partnership had been founded.

January 17, 2019

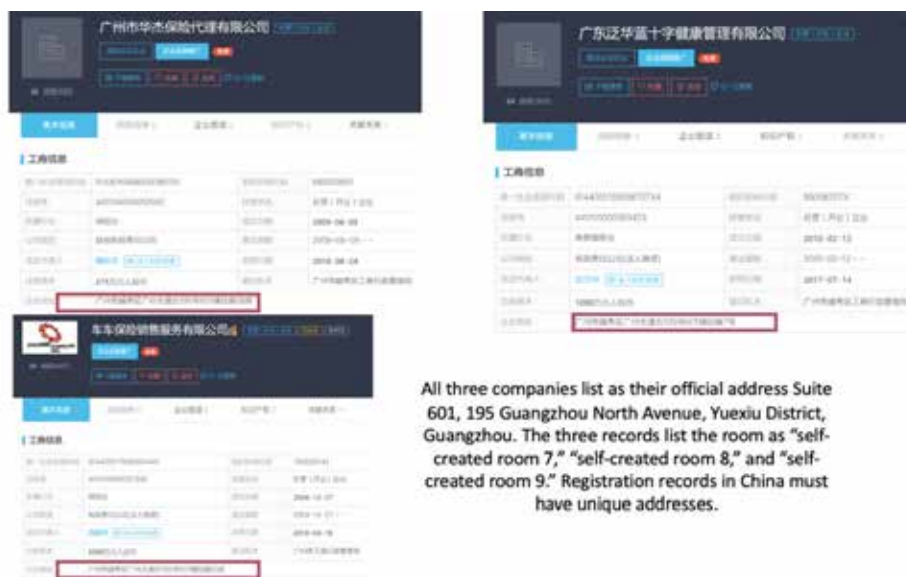
To see whether Shenzhen Ruiyuan does anything other than hold the investment in Cheche, we went to Shenzhen. But Shenzhen Ruiyuan has no staff, no phone, and has not kept its registration current with the government. This is common with fraudulent companies, which exist to facilitate capital transactions but not to engage in business.



This is the Shenzhen government agency that handles registration and bookkeeping for companies for a fee and where six Fanhua subsidiaries have their registered addresses. Shenzhen Ruiyuan Investment Co., an early investor in Cheche, also has its registered headquarters here, as does Chengchuang, the fund management company owned by Fanhua founder Lai Qiuping. | Photo by J Capital December 7, 2018

The fact that this investor in Cheche is co-located with Fanhua and Fanhua-related companies provides an additional piece of evidence supporting our view that Cheche has an undisclosed relationship to Fanhua. There is more: Three of Cheche's operating companies in Guangzhou share an office with two Fanhua companies and a company owned by Fanhua co-founder Lai Qiuping.

January 17, 2019



All three companies list as their official address Suite 601, 195 Guangzhou North Avenue, Yuexiu District, Guangzhou. The three records list the room as "self-created room 7," "self-created room 8," and "self-created room 9." Registration records in China must have unique addresses.

Registration records for Guangzhou Huajie Insurance Agency, wholly owned by Lai Qiuping, Guangdong Fanhua Bluecross Health Management Co, 100% owned by Fanhua, and Cheche Insurance Sales and Service, owned by Cheche. Source: State Administration of Industry and Commerce accessed December 20, 2018

Cheche's website (www.chetimes.com) has several photos of Cheche's office.

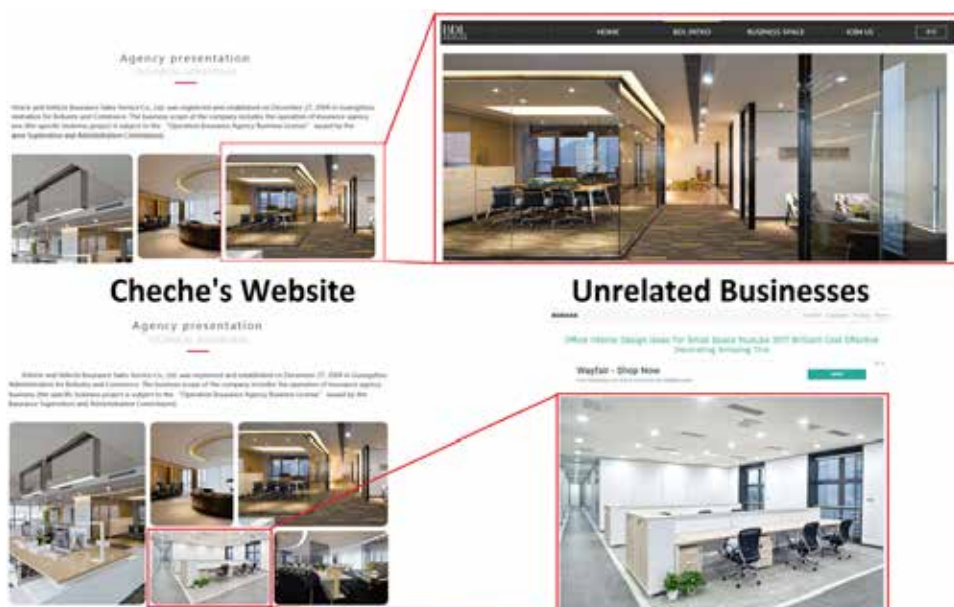


In November 2018, our investigator visited the office of Fanhua Times, which had supposedly been divested to Cheche in October 2017. At the office address, 601-09, No. 195, Guangzhou Ave, Yuexiu District, Guangzhou,¹⁰ our investigator was unable to find any location that looked like the photos on the website. The investigator also could not find the name and/or logo that Cheche uses on its website. Instead, the office displayed Fanhua's logo. We can only conclude that the company used stock images on its website to hide the fact that the office is still under the control of Fanhua.

Our investigator found several of the "Cheche office" images on websites of separate unrelated companies.

¹⁰ 广州市越秀区广州大道北 195 号 601 铺自编 09 房

January 17, 2019



Screenshots from Cheche's website and from unrelated sites.



The Cheche address. Source: China investigator, October 2018

Not the first fake transaction

The Cheche transaction was only one of many Fanhua deals that are not what they appear to be. Yang Lin, the executive who took over 11 of the companies purportedly sold to Cheche, has regularly received companies from Fanhua without disclosure of a related-party transaction. In 2017-18, Fanhua made undisclosed transfers to Yang Lin of four other companies in addition to the 11 transferred as part of the Cheche transaction. Those were Wenzhou Huilian, Shenzhen Nanfeng, Beijing Ruisike Management Consulting Co. Ltd., and Fanhua Bocheng Insurance Brokerage Co. Ltd.

- In January 2017, Fanhua reported divesting Beijing Ruisike Management Consulting Co. Ltd. to a third party. The company was actually transferred to Yang Lin.

January 17, 2019

- ▶ On July 10, 2018, Fanhua transferred Shenzhen Nanfeng Insurance Co. Ltd. to Yang Lin's Sichuan Boxin Xinrui. Shenzhen Nanfeng Insurance had been founded by Fanhua CEO Wang Chunlin and was purchased by Fanhua in 2014.
- ▶ On August 3, 2018, Fanhua transferred Wenzhou Huilian Insurance Agency to Yang Lin's shell company Sichuan Boxin Xinrui. Fanhua made no disclosure. Fanhua had acquired Wenzhou Huilian Insurance for ¥16 mln in 2014.
- ▶ On August 21, 2018, Fanhua announced that it was divesting Fanhua Bocheng Insurance Brokerage Co., Ltd. to a third party. In reality, Fanhua Bocheng was given to Yang Lin's shell company Beijing Boxin Lintong.

We obtained tax records for Shenzhen Nanfeng, Wenzhou Huilian, and Fanhua Bocheng Insurance Brokerage. Their 2017 revenue was \$30.3 mln, bringing the 2017 revenue of companies transferred to Yang Lin's ownership to \$135.96 mln.

Round trip

The Bocheng transaction is textbook legerdemain that took assets from Fanhua investors and put them under control of undisclosed related parties that we believe are proxies for top management. It worked like this:

1. In January 2017, Fanhua reported divesting a subsidiary called Beijing Ruisike Management Consulting Co. Ltd. to a third party.¹¹
2. In April 2017, Fanhua transferred Beijing Ruisike Management Consulting to Yang Lin.
3. In November 2017, Fanhua reported disposing of Fanhua Bocheng Insurance Brokerage to a third party. The disclosure from Fanhua's 20-F is as follows:

In November 2017, the Group disposed of Bocheng to a third party for a total consideration of RMB46,582. And the consideration receivable was further offset by the other payables to Bocheng . . . The Group recognized loss of RMB904 on the disposal of this subsidiary. (page F-28, Fanhua 20-F filed April 20, 2018. Numbers are in thousands.)

¹¹ "In January 2017, the Group disposed of Beijing Ruisike Management Consulting Co., Ltd to a third party." (2017 20-F page F-28, filed April 20, 2018).

January 17, 2019

4. Fanhua Bocheng was actually transferred to Beijing Ruisike Management Consulting and Beijing Boxin Lintong Technology Co. Ltd. By this time, Yang Lin owned both companies.
5. On November 22, 2017, Yang Lin transferred his equity in Beijing Ruisike Management Consulting to Liu Tingting. This transaction was undisclosed. Liu Tingting calls herself a Fanhua employee, and we believe she is a stand-in for top management.

In this way, both Beijing Ruisike Management Consulting and Fanhua Bocheng Insurance Brokerage were removed from the Fanhua balance sheet and are now privately controlled by Fanhua executives.



Source: SAIC via Qixin



A photo of Liu Tingting posted on the Yongyong social networking sites. The title given is "Fanhua Finance Sales Director." | Access at this URL: <https://mimai.cn/contact/share/card?u=2hnafdm00gavr&from=singlemessage>

So who is Liu Tingting, who now owns two companies that Fanhua "divested" in 2017 and 2018? Three separate interviews in Beijing confirmed that she is a Fanhua employee. Furthermore, in Liu Tingting's social profile, she calls herself "Fanhua Finance Sales Director." A [job ad](#) for Ruisike, Liu Tingting's company, says that Ruisike has "the managerial strengths and capital of the Fanhua Group."

January 17, 2019



The building directory lists two Fanhua companies, Beijing Fanlian Insurance Sales Agency Co. Ltd. and Fanhua Lianxing Insurance Sales Agency, Beijing Branch



Entrance to Fanhua office on 9th floor of 5 Xiangjun South in Chaoyang District. | Photo by J Capital December 21, 2018.

Ruisike Management Consulting is located with 10 other Fanhua companies in a building called the Yulin Mansions in Beijing, where Fanhua companies are registered on the 6th, 7th, 9th, and 20th floors.¹² Three of

¹² The building is the Yuxia Mansion at No. 5 Xiangjun South in Chaoyang District. The companies are:

- 1) Beijing Ruisike Management Consulting Co. (北京瑞斯科管理咨询有限公司) on floor 6, Room 703
- 2) Fanhua Lianxing Insurance Sales Co. (泛华联兴保险销售股份有限公司) on floor 8, Room 903
- 3) Beijing Fanhua Investment Co. Ltd. (北京泛华投资有限公司) on floor 6, Room 701
- 4) Beijing Fanlian Insurance Agency Co., Ltd. (北京泛联保险代理有限公司) on floor 7
- 5) Fanhua Times Insurance Sales Beijing Branch No. 1 (泛华时代保险销售服务有限公司北京第一分

January 17, 2019

the floors, 7, 9, and 20, were occupied, though we could not find people in the offices on a Friday afternoon. All three offices displayed the sign “Fanhua Insurance Services.” There was no sign for Beijing Ruisike.

Beijing Ruisike appears to exist on paper only, but its subsidiary, Fanhua Bocheng, seems to be going strong. In fact, it still operates as Fanhua—it’s just not owned by Fanhua anymore. Beijing Bocheng’s [web page](#) says that the company is owned by Fanhua. This text from the About Us page of Bocheng’s website, accessed on January 4, 2019, reads as follows:

+ 公司简介 您现在的位置: 首页 > 关于我们 > 公司简介

泛华博成保险经纪有限公司（以下简称“泛华经纪”）于2005年1月12日成立，总部设在北京，注册资本金5000万元人民币。已发展为国内领先的综合性保险经纪服务平台。

泛华经纪属于全国性的保险经纪公司，可为全国各地客户提供专业的保险经纪服务；并依托集团的资本优势和管理优势，为全国各地客户提供全方位的保险中介服务。服务领域包括：覆盖广泛的大型商业风险、寿险经纪、责任险和信用险、风险咨询评估和管理、再保险经纪业务；服务行业覆盖：国家战略储备物资、国家行业协会、石油、交通、运输、进出口贸易、仓储、建筑工程等一切涉及到风险管理和风险转移的行业。

“Fanhua Bocheng Insurance Brokerage Co. Ltd. (hereafter called “Fanhua Brokerage”) was established on January 12, 2005 and is headquartered in Beijing with ¥50 mln in registered capital. The company has already developed into a leading comprehensive insurance brokerage platform.”

These transactions rob shareholders of value.

Lining the Founder’s Pockets

Last June, Fanhua launched a share compensation scheme that we believe is a decoy for self-enrichment. To kick off the plan, Fanhua purchased 8.5 mln shares from its co-founder, Lai Qiuping, at \$29 per share, giving Lai \$246.5 mln, ostensibly in order to create a “bank” of shares that can be awarded to employees in the future.

We do not believe employees will realize a benefit. The incentive plan is probably illegal in China and therefore not really intended to be imple-

-
- 公司) on floor 6 Room 701 (*Note that this company has been sold to Beijing Cheche)
- 6) Fanhua Times Insurance Sales Beijing Branch No. 2 (泛华时代保险销售服务有限公司北京第二分公司) on floor 6, Room 710
- 7) Shenzhen Fanhua United Investment Group Beijing Consulting Branch(深圳泛华联合投资集团有限公司北京咨询分公司) on floor 20, Room 2002
- 8) Xinzhiming Asset Management (Beijing) Co., Ltd. (鑫智盈资产管理(北京)有限公司) on floor 3 (This is a company owned by Fanhua co-founder Lai Qiuping, company executive Yang Lin, and a third person named Fan Ming.)
- 9) Litian Zhuoyue Software (Beijing) Co., Ltd. (力天卓越软件(北京)有限公司) on floor 6, Room 703
- 10) Beijing Fanhua Small Loans Co. Ltd. (北京泛华小额贷款有限公司) on floor 20, Room 2001 (This is a privately owned company with ostensibly no ownership link to Fanhua.)
- 11) Beijing Fanhua Insurance Agency Co., Ltd. (北京泛华保险代理有限公司) on floor 7

January 17, 2019

mented. And Fanhua has a history of stiffing employees on these share schemes. Fanhua has not explained why it needs to purchase all shares for the incentive plan outright, instead of having employees purchase them directly. And Fanhua has only barely enough cash to make the purchases. Fanhua spent fully 78% of its cash and cash equivalents to purchase shares. Finally, the price paid to Lai is too high: the trading price of the shares has been as low as \$21 since June. Fanhua shares are currently trading at about \$23.

Last June 15, Fanhua announced the “521 Development Plan” to award shares to employees as incentive for meeting sales targets over the coming five years. We obtained a copy of the Power Point presentation given to employees to encourage them to join.



Cover from Fanhua's share incentive plan deck. Source: Fanhua employee

521 is very unusual for an equity incentive plan. It establishes three funds that each will purchase 14 million shares of the Nasdaq-traded stock. Fanhua is providing loans to support the exercise price of the shares, which is \$29. Employees are to pay 8% on the loans, in cash.¹³

- **We believe the plan is illegal:** It is technically illegal under China's foreign-exchange rules for Chinese citizens to own foreign company

¹³ There are eligibility criteria attached to sales targets each year.

January 17, 2019

shares, unless the ownership is approved by the State Administration of Foreign Exchange. The necessary approvals are not transparent, and to our knowledge, have never been granted. Foreign companies frequently structure their plans to provide "phantom" stock option grants, i.e. the right to receive the difference between the strike price and the exercise price of a stock option. Technically, that spread is supposed to be given to employees in Renminbi and is subject to standard individual income tax rates. Although these rules have not often been observed, direct share grants are probably not legal.

- ▶ **Why the private transaction?** Fanhua could have bought shares on the open market, which would have benefitted all shareholders.
- ▶ **The loan component also looks illegal:** As part of the 521 Plan, Fanhua reported that it would grant up to \$365.4 mln in loans to its own employees at 8% interest to fund their purchases of the shares. This is firmly illegal in China. Interest-bearing loans to employees are considered "illegal fundraising," while extending loans in Renminbi to fund assets that are priced in dollars is a foreign exchange activity permissible only to government banks.
- ▶ **The share awards are contingent, but the shares have been purchased outright:** To be eligible for the share incentive plan, managers must achieve certain thresholds of life insurance policy sales starting with 1.2 mln and going to 5 mln per year. That there are targets suggests that not all participants will be eligible for shares, yet Fanhua has pre-purchased the shares for the incentive plan.

The plan itself invites potential participants to become "franchisees" and tells them that they may choose between joining Fanhua and running their own company. This would seem to contradict the company's assertion that it owns all the agencies directly. Slide 11 reads:

Fanhua's Entrepreneurship System

Five characteristics:

1. Being an entrepreneur makes you happier
2. High performance bonuses
3. Employment for life
4. The benefits for joining the franchise are good
5. High profits for founding a company

January 17, 2019

And four additional points:

1. You are the customer
2. The team is yours
3. The team can be inherited
4. The team can be handed over

In brief, Fanhua represents itself to investors as a directly owned insurance sales team. But the company represents itself to outsiders as a network of independently owned companies flying one corporate banner.

We offer two alternative explanations for the mysterious 521 Plan:

- ▶ Maybe Fanhua does not actually have the cash it claims. A curious line on the balance sheet, called short-term investments, ballooned from ¥688 mln in 2014 to ¥2 bln in 2015 without explanation and despite slow revenue growth and anemic cash generation. We cannot understand how Fanhua can generate that much cash on such low profitability. If Fanhua were overstating its cash balance, using the phantom cash to “buy shares” from Lai, this might be one convenient way to remove it from the balance sheet.
- ▶ Fanhua may want to book 8% interest income on the loans that Fanhua advertises it will extend to participating employees, an amount that should garner around \$20 mln per year. The company has said it would lend \$365 mln toward the share options.

Déjà vu all over again

The “521 Development Plan” looks a lot like the share incentive scheme that torpedoed Fanhua’s share price in 2010-11.

Fanhua, formerly called CNInsure (CISG US), has consistently found itself unable to offer both attractive sales compensation and high profits that would send the share price higher. Consequently, Fanhua concocted a compensation scheme that it kept secret from public investors and failed to book as a cost.

In 2010, a research company called OLP found that Fanhua had issued equity incentives to its managers without disclosing the arrangement to investors. After the detailed report came out, Fanhua vehemently denied the share plan despite ample evidence from Fanhua’s own website.

January 17, 2019

Chart 3. Fanhua price chart from inception until the OLP report



Source: Bloomberg

Chart 4. Fanhua share price between OLP report and 2014



Source: Bloomberg

In spite of the continued denials, after issuance of the OLP reports, Fanhua's reported growth and margins collapsed, suggesting that canceling the share incentive plan had exposed Fanhua's operating reality. Net income declined by 171% in 2011 compared with 2010, falling to negative ¥299 mln (-\$43 mln). By 2016, net income was still just 37% of what had been claimed in 2010.

Management tried and failed to take the company private, with the deal collapsing when a PE firm that had reportedly spent millions on due diligence backed out of the deal. [A Financial Times article](#), "Foreign investors

January 17, 2019

negotiate Chinese minefield,” published on November 29, 2011 claimed that a private equity investor had spent \$10 mln on due diligence then backed out of the deal.

[The 521 Development Plan](#) looks very much like the share incentive plan that Fanhua failed to disclose in 2010.



J Capital translation of part of the 521 Plan slide presentation. Stage 1 of the plan: “2016-2018: Net profits reach CNY 500 million and the share price increases from USD 7 to USD 35.” In 2019-2021, the plan says, “the share price increases from USD 35 to USD 100.”

The promise of future share compensation may have raised apparent profits by diverting bonus or commission. With 0 revenue growth in 2017, Fanhua reported 169% growth in profit. That profit came principally from a 56% decline in selling expenses—even though the company more than doubled its headcount of sales representatives, from 231,592 to 579,348.¹⁴

Fanhua assures its employees that the company is putting resources into the share incentive plan, which they call the “happy struggle plan”:

¹⁴ See FANH 2017 20-F filed April 20, 2018, page 26

January 17, 2019



Fanhua 521 Plan slide, J Capital translation. Readers can download the presentation with J Capital's translation [here](#).

Enriching insiders, stiffing shareholders

The Cheche sale was only the latest in double dealings by Fanhua, which habitually enriches its executives by giving them investor-financed loans, equity in affiliates, or cash. In the bullet point below, we list 14 historical examples, but they are far from exhaustive.

Fanhua says that it directly owns 100% equity in all of its insurance intermediary companies. This is patently untrue. The company disclosed that its restructuring began in 2011 and was undertaken because of a regulatory change in China that made it easier for a foreign-owned firm to own insurance agencies. "... in October 2011 we commenced a restructuring of our company which resulted in us obtaining direct controlling equity ownership in all of our insurance intermediary companies." (Page 15, 2015 20-F)

Then, in a 6-K filed on May 25, 2016, the company reported:

As of date, except for two insurance agencies and the claims adjusting operation, we have completed acquiring the minority interests of all of our insurance intermediary companies.

But this is not true. Post May 2016, we identified nine employees with shareholdings in 33 Fanhua companies. This is far from an exhaustive list and does not count employees with independent companies that engage in undisclosed related-party transactions with Fanhua. Here are just a few examples:

January 17, 2019

- ▶ Fanhua holds 55% of Hunan Fanhua Insurance Agency, while the company's Hunan regional manager, Cheng Huiqi, owns 20%. Another 15% is held by a Fanhua employee involved in many of the Puyi companies named Sun Conghai, and 10% by another Fanhua employee named Zhu Jiusheng.¹⁵ The company, according to our interviews, was set up by Fanhua, which then awarded equity to managers. Chen Huiqi's 2008 appointment as regional manager was announced by China's insurance regulator
- ▶ Hebei Fanhua Insurance is 12.5% owned by a holding company that belongs to a current or former Fanhua employee named Xue Kai.¹⁶
- ▶ Tianjin Jingxu Investment, owned by two individuals, has invested in and divested from eight Fanhua companies. The Tianjin company bought 45% of Hubei Fanhua Insurance Agency, Co., for example, and sold the equity back to Fanhua in 2015. Although Fanhua did not report the details, it did report its ownership of Hubei Fanhua, a company with 13 branches in the province, going from 55% to 100%.

The companies typically use many layers of ownership that make it impossible for shareholders to understand what they actually own. In the case of Hubei Fanhua, there are six layers of companies between CNInsure Holdings, the ultimate parent, and Hubei Fanhua, and 11 different Fanhua entities have interests in the Hubei company. Furthermore, the equity shifts around year to year.

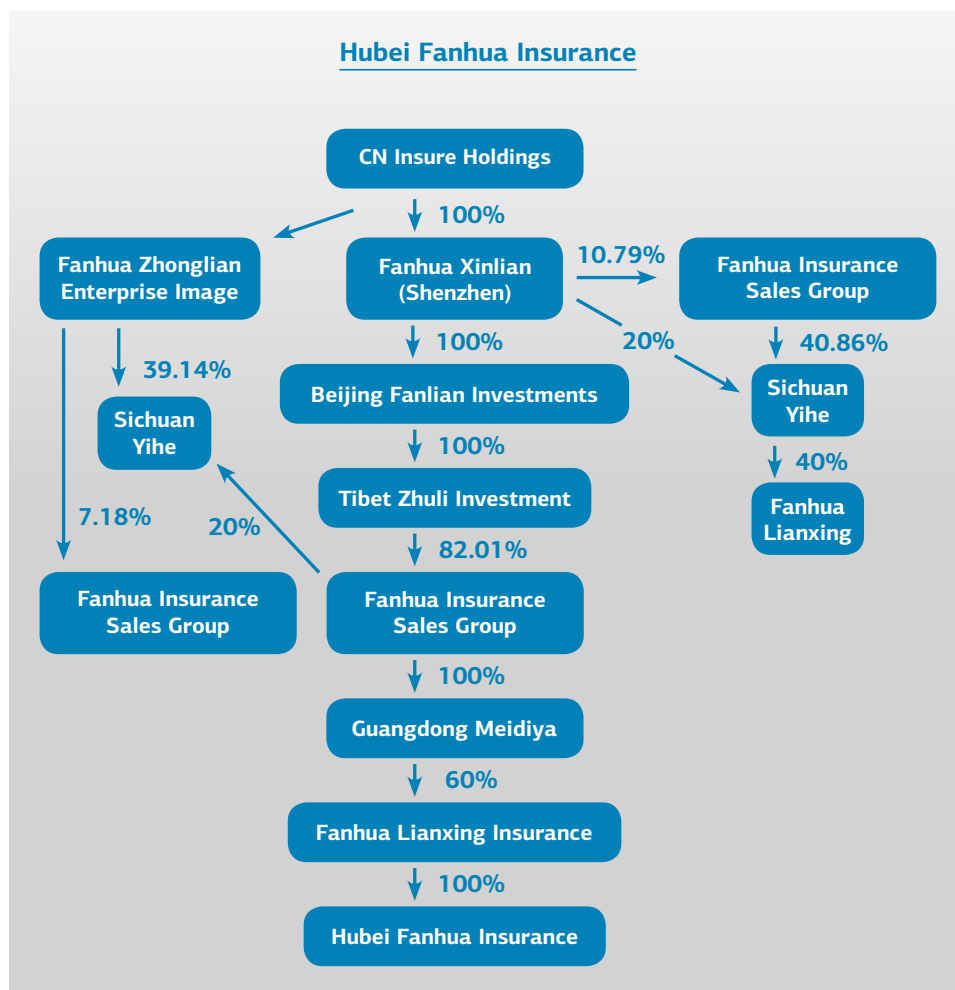
While the fact that there are minority interests is often disclosed, Fanhua does not tell investors that the minority owners are Fanhua employees. The self-dealing has gone on throughout the history of the company.

- ▶ Top Fanhua executive Sun Conghai sold the majority of the Hebei province operation to Fanhua in two transactions, one in 2009

¹⁵ See the corporate registration record here: <https://www.tianyancha.com/company/768446195> or here: <https://www.qixin.com/company-chart/structure/d59148cb-25da-47f9-9cab-4b67af69eb45> (registration needed). This Tianya post describes the role of Sun Conghai: <http://bbs.tianya.cn/post-enterprise-550699-1.shtml>. Zhu Jiusheng is a director of a Fanhua-owned company called Fan Financial Investment Co. Ltd. that is registered in Tibet. He is also an owner, director, or manager of 13 companies related to Lai Qiuping. Government records showing his corporate relationships can be found here: <https://www.qixin.com/name-detail/2f1418508059f8cfd7cbb80590bc36f7> (subscription needed).

¹⁶ The Fanhua Holdings website provides a history of Xue Kai's employment: <http://www.fanhua-holdings.com/cyvj/cygs/A20071106506.shtml>. Also see this article on Sohu in 2010 in which Fanhua CFO Ge Peng announced Xue Kai's appointment: <http://money.sohu.com/20100813/n274197162.shtml>

January 17, 2019



Source: Company disclosures, Chinese State Administration of Industry and Commerce, J Capital

and the other in 2015. According to our interviews, Sun Conghai is founder of Fanhua's Puyi Fund company. He is described in this BBS post as a top executive of Fanhua.¹⁷

- ▶ A former Fanhua vice president called Xue Kai owns 12.5% of Hebei Fanhua. Xue Kai is a senior executive officer whose term ran from January 1, 2007 to December 31, 2011. In various interviews that have appeared in the Chinese press, company executives described Xue's role as driving a newly consolidated life insurance business. According to our interviews in the insurance industry in Hebei Province, Xue founded an insurance sales agency in Hebei in 2005 and

¹⁷ Fanhua originally owned 10% of Hebei Fanhua. It bought an additional 41% in 2009 (FANH 6-K filed March 3, 2010) without disclosing how much it had paid, and, in 2015, it acquired an additional 36.5% of the equity interest for a total consideration of \$6.5 million in cash and a 12.5% share of profit or loss in the Hebei operations (FANH 6-K filed May 20, 2015).

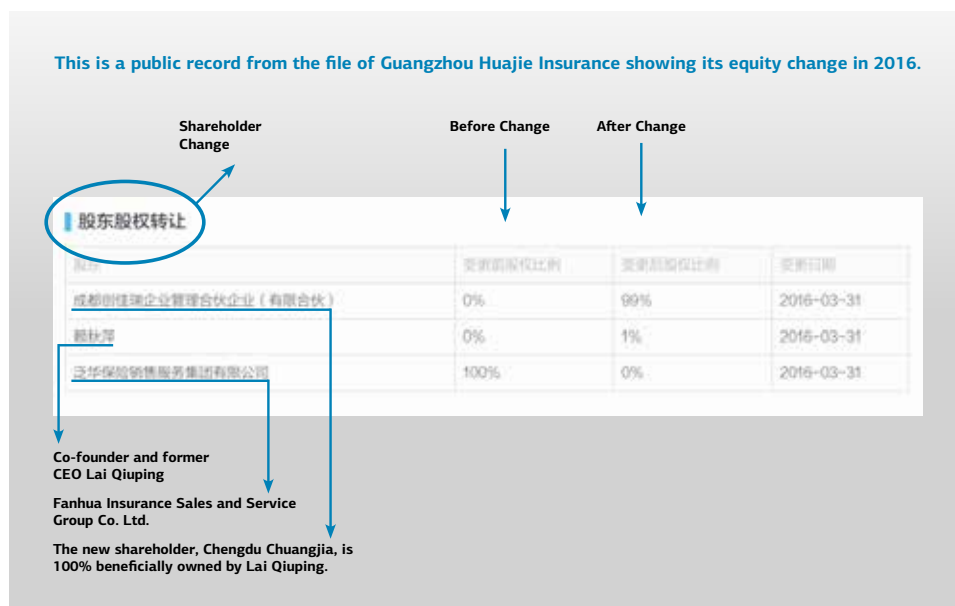
January 17, 2019

joint ventured with Fanhua in 2009. Chinese government records show that he is a current or past owner or executive of 17 companies, of which at least seven are Fanhua companies.

- ▶ In 2008, three executives of Hunan Fanhua Insurance Agency were granted 45% of the company's equity.
- ▶ In the province of Hubei, Fanhua similarly compensated executives. Fanhua established Hubei Fanhua in 2004 as a wholly owned subsidiary and then hived off 40% of the equity for executives Zhu Jiusheng and Long Yubo. Fanhua bought back the equity from them in December 2015, according to Chinese corporate records.
- ▶ Between December 2015 and September 2016, Fanhua purchased equity in five Fanhua companies from Long Yubo, who was described in 2015 as a vice president of the fund company and holds his equity via a Tianjin-registered company called Tianjin Jingxu.
- ▶ In August 2009, Fanhua purchased equity in Jilin Fanhua from company executives Long Yubo and the fund founder Sun Conghai. Fanhua sold the equity again in 2014 to an individual named Wang Yu. The company's name was changed to Jilin Ronghao Insurance.
- ▶ In July 2010, Fanhua paid about \$13 mln to acquire limited "preference rights" to Shenzhen InsCom E-Commerce, a company whose ultimate beneficiary appears to be Fanhua CEO Wang Chunlin.¹⁸
- ▶ In 2011, the company paid its co-founder and president Lai Qiuping about \$7.9 mln for two companies he owned, Guangzhou Huajie and Dongguan Zhongxin, which Fanhua then divested in 2016 for about \$30,000.
- ▶ In February 2013, Fanhua purchased equity in Sichuan Fanhua Xintai Insurance from executive Zhu Jiusheng.
- ▶ In June 2014, Fanhua purchased Nanjing Yukai Insurance from Sun Conghai.

¹⁸ See FANH 6-K filed July 30, 2010 page 6: "... CNinsure will acquire 65.1% equity interest in InsCom for RMB84 million. Meanwhile, as part of the corporate restructuring of InsCom, CNinsure's equity interests in six of its affiliated property & casualty insurance agencies will be transferred to an affiliated subsidiary of InsCom in exchange for preference shares newly issued by InsCom. With the preference shares, CNinsure is entitled to all of the profits of InsCom for a certain period and reserves the right to require InsCom to redeem the preference shares."

January 17, 2019



Source: Chinese State Administration of Industry and Commerce

- ▶ In July 2015, Fanhua purchased equity in Changsha Lianyi Insurance and Ningbo Baolian Insurance from Sun Conghai
- ▶ In October 2015, Fanhua bought equity in Shandong Daoxing Mintai from Sun Conghai and sold it the next year to Shandong Dongsan International Holdings.
- ▶ In December 2015, Fanhua bought equity in Henan Fanhua Anlian from Sun and Zhu.
- ▶ In 2016, Fanhua disposed of Guangzhou Huajie Insurance Agency to its co-founder, Lai Qiuping. Fanhua had purchased the company in 2011 for ¥25 mln. The company has not disclosed the disposal as a related-party transaction.
- ▶ In January 2016, Chinese records show that Fanhua transferred its equity in Hebei Fanhua Insurance Agency Co. Ltd., with six branches, to two private owners. The owner of 87.5% of the equity is a Fanhua executive, even though the company is identified on the Fanhua Holdings website as a Fanhua subsidiary.
- ▶ In 2016, Fanhua bought Fanhua Century Insurance Agency from a holding company owned by its CEO, Wang Chunlin.¹⁹

¹⁹ Chinese SAIC records show that Fanhua Insurance Sales Agency Group Corp. acquired Shenzhen Xinbao Investment Co. Ltd. from Wang Chunlin and two minority owners. Shenzhen Xinbao was the owner of Fanhua Century Insurance.

January 17, 2019

- ▶ Fanhua has extended ¥500 mln in loans to Shenzhen Chuangjia Investment Limited Partnership, owned by company executive Yu Haifeng,
- ▶ In July 2018, Fanhua sold or transferred its wholly owned subsidiary Guangzhou Yian Insurance Agency to Yang Lin's Boxin Xinrui. Fanhua Times had injected capital in April 2017. The company's last disclosure about this company was in 2012.

Fanhua made the loan to Shenzhen Chuangjia without disclosing that Chuangjia is a related party. The disclosure in the 2017 20F is as follows:

This (other receivables RMB 513 million) represented loan to Shenzhen Chuangjia Investment Partnership Limited ("Chuangjia") of RMB500 million and corresponding interest receivable RMB13.18 million. The loan is secured by the 99% equity share of Chengdu Puyi Bohui Information Technology Limited ("Puyi Bohui"), a major operating subsidiary of Chuangjia, with interest rate 7.3% per annum.

Our investigator visited Shenzhen Chuangjia and found that it displays the CNFinance logo. The company is headquartered at its 1901, Luohu Business Center, No. 2028, Shennandong Road, Luohu District, Shenzhen.²⁰

Based on Chinese government records, Shenzhen Chuangjia is 99.99% beneficially owned by Yu Haifeng, the CEO of [Puyi Inc.](#), a P2P platform associated with FANH.

FANH did not disclose the relationship between Chuangjia and FANH even though Chuangjia is controlled by Yu Haifeng, who is the CEO of a related party. Therefore, Chuangjia is actually an undisclosed related party to CNFinance and also FANH.

Fanhua's [official website](#) in China lists the major subsidiaries in each province as well as a few cities. There are 210 companies listed. We looked up the registration records of most. The majority are either not owned by Fanhua at all or have equity holders who are individuals.

For example, randomly choosing Wenzhou in Zhejiang on "The Fanhua organization" portion of the Fanhua website, the life insurance company listed is Wenzhou Huilian Insurance. This company is owned by Yang Lin.

²⁰ 深圳市罗湖区深南东路 2028 号罗湖商务中心 1901 单元 (入驻深圳泛华基金管理服务有限公司)

January 17, 2019



Offices of Shenzhen Chuangjia. Source: China investigator October 2018

"The Fanhua Organization"

泛华机构



机构介绍

Wenzhou

Life insurance: Wenzhou Huilian Insurance Agency, Lucheng District, Wenzhou

寿险

温州惠联保险代理有限公司

地址: 温州市鹿城区车站大道京龙大厦1幢十一层2号-1、十二层

电话: 0577-86799157

Registration record for Wenzhou Huilian Insurance Agency, from the State Administration of Industry and Commerce

Five branches

公司名称	负责人
温州惠联保险代理有限公司温州第二分公司	王露
温州惠联保险代理有限公司龙湾永中营业室	孔令明
温州惠联保险代理有限公司龙湾分公司	陈奇峰
温州惠联保险代理有限公司乐清分公司	郭志敏
温州惠联保险代理有限公司瑞安分公司	陆光

Beneficial owner

受益所有人

序号	受益所有人名称	持股比例	持股比例数量	操作
1	杨林	99%	1	展开

Yang Lin

Source: Above: Fanhua Holdings website Below: State Administration of Industry and Commerce via Qixin

January 17, 2019

Fanhua shareholders are not the owners of around half of the companies listed on Fanhua's official website. The companies sold to Cheche are still displayed on the site, with addresses and phone numbers. In Guangzhou, Guangzhou Huajie is shown as a sales agency, and yet this company is wholly owned by Lai Qiuping.

Undisclosed guarantees

Our interviews indicate that Fanhua is paying handsome returns to one of its founders for capital raised from the public. Fanhua employees and former employees we interviewed confirmed that Fanhua guarantees financial products issued by Lai Qiuping's Chengchuang (Shenzhen) Investment Co. Ltd. We have identified 41 such investment products. Funds offered to the public have to be registered with China's securities regulator, and the fund minimum issuance value is ¥10 mln. That means that total issuance is at least ¥400 mln (\$58.3 mln). But we believe that Lai's company has raised several times that amount. A Fanhua interviewee told us that the guaranteed products outstanding have principal of "at least ¥1 bln (\$147 mln)" and that Fanhua guarantees returns of 6.8%-8.5%.

Fanhua explicitly claims it does not issue guarantees. On page 67 of its 2017 20-F, the company says "We have not entered into any financial guarantees or other commitments to guarantee the payment obligations of third parties." But four separate longtime employees of Fanhua told us that the company does guarantee Lai's products. A sales agent also confirmed this and said the guarantee is in the purchase contract but that employees are not permitted to disclose the contract except to paying clients.

Some of this money appears to have been channeled into pre-IPO shares of Fanhua subsidiary CNFinance; although employees selling the Chengchuang funds did not know the specific investment targets, several of the investment products return as much as 150% to retail investors, according to Chinese government notices, and we cannot think of an investment other than pre-IPO shares that could reach that rate of return. But, given that Fanhua guarantees 8.5% on products issued for two years, the ¥1 bln or more should properly be recognized as debt and should be disclosed as such.

The "private equity" securities have bland names, like "Chengchuang M&A Fund No. 3." But our interviews indicated that the money is all being channeled into Fanhua to promote sales growth.

Chengchuang tells investors that its funds return as much as 144%. Below is a liquidation notice issued on September 28, 2018 for the "Chengchuang

January 17, 2019

M&A Phase 6 Equity Investment Fund,” launched May 19, 2016. The notice reports that the fund returned 143.74% to subordinated investors and 45.66% on the preferred tranche.



Liquidation notice. Source: Fanhua investor

A mid-level employee at Fanhua told us the following in an interview (our translation): “Chengchuang Funds was founded to raise money for Fanhua Group. The principal use of funds is to support various Fanhua business units in their effort to achieve a listing in the United States.” This was corroborated in a second interview. Four other interviews confirmed that Fanhua guarantees both principal and returns on Chengchuang private equity funds.

Longtime Fanhua employees told us that “most” of the Chengchuang funds raised are invested in Fanhua. We have seen three Chengchuang fund liquidation notices signaling fund payouts, and each reported returns over 42% to preferred investors. Salespeople confirmed that this return is typical. Whether or not Fanhua itself has paid returns of that level to Lai’s company, Fanhua’s guaranteed 8.5% return constitutes both undisclosed debt and an undisclosed related-party transaction. In other words, the Chengchuang financial products are yet another way in which Fanhua management has lined its own pockets.

Several interviewees told us that the Chengchuang financial products all raise money for Fanhua subsidiaries. Those comments support our view that Fanhua is desperate for cash and that the cash balances reported in the company financial statements may not be reliable.

“The FANH co-founder’s company “was founded to raise money for Fanhua Group. The principal use of funds is to support various Fanhua business units in their effort to achieve a listing in the United States.”

January 17, 2019

Fanhua's secret real estate development

Fanhua has undertaken a massive commercial real estate project in Renshou, the county about 70 kilometers from Chengdu where company founder Hu Yinan was raised and that is host to at least five phantom Fanhua companies. Fanhua has not disclosed the investment except in the most general terms. Fanhua formed a 51-49% joint venture real estate development company on July 19, 2016 to develop 14 buildings with a construction area of 336,499 in the "Tianfu New Area." Fanhua and contributed just over ¥10 mln in capital but made no mention of the Tianfu project until November 5, 2018, when Fanhua issued a 6-K announcing that its life insurance operation had completed its relocation to Tianfu.

FANH is a 51% (majority) owner in this joint venture, which has not been disclosed. This should prompt the company's auditors to ask why the JV was not consolidated in FANH's financials. The company described the JV by saying:

"In addition, persuaded to its policy of attracting investment to develop the local economy, in 2016 the **Renshou County government** in which the Tianfu New Area is situated, expressed its support for **Fanhua** to publicly bid for a parcel of land in the Tianfu New Area to establish a back-office center. As Fanhua had neither a license nor interest in real asset development, on July 16, 2016 Fanhua established a joint venture with an independent third party real-estate developer Sichuan Tianyi Real Estate Development Company for the sole purpose of developing the parcel of land. Under this arrangement, Sichuan Tianyi will be responsible for developing the land and providing all funding for the development, while Fanhua will not provide any loan guarantee or any other funding for the development. Upon completion of the real estate development, Sichuan Tianyi would keep all the profits from the sales of the development properties and Fanhua will have a right to purchase certain properties at a discount. As of today, the project is still under development."²¹

We found it ridiculous that FANH is involved in, or may benefit from, this transaction, as they clearly disclose they:

1. Will not provide any loan guarantee

²¹ Company Q3 2018 conference call, Seeking Alpha transcript: <https://seekingalpha.com/article/4223777-fanhua-inc-fanh-ceo-chunlin-wang-q3-2018-results-earnings-call-transcript?part=single>

January 17, 2019



Photos of the Fanhua project and the sales room. Source: China investigator September 2018

2. Will not provide “any other funding” for the development
3. Don’t have a license
4. Don’t have an interest in real estate development

Despite FANH’s statement that they’re not funding the project, our due diligence has led us to believe that they are likely contributing capital to it, unbeknownst to FANH’s investors.

We became aware of the existence of this real estate investment and the [details of this project](#) back in the summer of 2018, during the course of our on the ground due diligence. Prior to the November 2018 conference call, FANH had never disclosed that it had a real estate investment associated with its relocation with Fanhua Lianxing.

项目简介

天府金融港位于天府新区城南高新技术产业区，紧邻天府大道，项目由**成都金控集团**投资开发，作为配套兴建的金融功能载体。天府金融港将与现有金融贸易、行政商务、文体会展等功能紧密结合，打造集“产、城、人、文”于一体的天府南园。天府金融港打造为160亩综合体，分为4大组团，林溪——跨境贸易总部、云玺——金融家会所、彩城——金融创客SOHO、红岸——立体魔方馆。规划3200亩生态湿地公园（在建中），林溪【跨境贸易总部】，于溪岸河畔，集5+1F跨境贸易、10+1F生态休闲及26F空中会所。

“The project is invested in and developed by **Fanhua Financial Holdings Inc.**”

Screenshot from the “Tianfu Finance Harbor” [website](#) on Fang.com. January 10, 2019

Fanhua has undertaken the project in a joint venture with a Sichuanese developer called Tianyi Real Estate, and the housing is already being pre-sold, with earliest delivery scheduled for December 2020, according to our interviews with salespeople.

But the [project website](#) says that Fanhua Inc. is the developer.

January 17, 2019

Sell

We believe that Fanhua is designed as a stock promote. Nothing has changed except the share price since the company was exposed in 2010 and sued by shareholders. We believe this company will go to zero and delist.

January 17, 2019

Appendix A

Actual acquirers of companies targeted for sale to Beijing Cheche Technology and 2016-17 company revenue

Target Companies	Chinese Name	2018 Ownership	2017 Revenue (USD)	2016 Revenue (USD)
Beijing Fanlian Insurance Agency Co., Ltd.	北京泛联保险代理有限公司	Cheche	\$0	\$0
Beijing Fanhua Insurance Agency Co., Ltd.	北京泛华保险代理有限公司	Cheche	\$0	\$0
Beijing Fanhua Fumin Insurance Agency Co., Ltd.	北京泛华富民保险代理有限公司	Cheche	-	\$0
Tianjin Fanhua Xianghe Insurance Agency Co., Ltd.	天津泛华祥和保险代理有限公司	Boxin Xinrui	\$452,203	\$281,091
Hebei Fanlian Insurance Agency Co., Ltd.	河北泛联保险代理有限公司	Boxin Xinrui	\$1,153,855	\$3,777,819
Shenyang Fangda Insurance Agency Co., Ltd.	沈阳方大保险代理有限公司	Boxin Xinrui	\$700,975	\$1,502,540
Nanjing Yukai Insurance Agency Co., Ltd.	南京誉凯保险代理有限公司	Boxin Xinrui	\$339,067	\$1,222,493
Hangzhou Fanhua Zhixin Insurance Agency Co., Ltd.	杭州泛华执信保险代理有限公司	Cheche	\$1,697,107	\$2,681,353
Ninbo Baolian Insurance Agency Co., Ltd.	宁波保联保险代理有限公司	Boxin Xinrui	\$11,623,598	\$11,006,454
Jiaxing Lianbao Insurance Agency Co., Ltd.	嘉兴联保保险代理有限公司	This company is co-owned by Fanhua and Cheche, with 70% held by Cheche and 30% by CNInsure Holdings.	\$1,337,356	\$4,327,405
Wenzhou Baolian Insurance Agency Co., Ltd.	Cannot identify a company with this name.	Company does not appear to exist		
Henan Fanhua Anlian Insurance Agency Co., Ltd.	河南泛华安联保险代理有限公司	Boxin Xinrui	\$14,150,565	\$33,235,907
Changsha Lianyi Insurance Agency Co., Ltd.	长沙联益保险代理有限公司	Cheche	\$5,078,957	\$8,036,696
Guangdong Nanfeng Insurance Agency Co., Ltd.	广东南枫保险代理有限公司	Boxin Xinrui	\$16,793,925	\$18,394,189
Guangzhou Fanhua Yi'an Insurance Agency Co., Ltd.	广州市益安保险代理有限公司	Boxin Xinrui	\$2,260,654	\$2,471,875
Dongguan Nanfeng Jiayu Insurance Agency Co., Ltd.	东莞市南枫佳誉保险代理有限公司	Boxin Xinrui	\$17,245,391	\$20,716,842
Foshan Tuohua Insurance Agency Co., Ltd.	佛山市拓华保险代理有限公司	Cheche	\$5,223,982	\$5,878,843

January 17, 2019

Target Companies	Chinese Name	2018 Ownership	2017 Revenue (USD)	2016 Revenue (USD)
Jiangmen Fanhua Zhicheng Insurance Agency Co., Ltd.	江门泛华智诚保险代理有限公司	Boxin Xinrui	\$742,755	\$978,090
Fanhua Kafusi Insurance Brokerage Co., Ltd.	泛华卡富斯保险经纪有限公司深圳分公司	Boxin Xinrui	\$11,556,292	\$31,021,550
Total of companies transferred to Yang Lin via Sichuan Boxin Xinrui			\$ 95,007,427	\$124,608,850
Total of companies sold to Cheche			\$ 12,000,046	\$16,596,892
Total Other Companies			\$ 1,337,356	\$4,327,405
Total			\$ 108,344,829	\$145,533,147

Source: Chinese Tax Authorities

Appendix B

Interviews of the Companies Targeted for Sale

Company 1	No working number could be found for this company through Baidu or public databases.
Company 2	The company was aware it had been sold to Cheche. "We sell very little life insurance, almost all auto insurance. Our business is the same, but the name we now use is Cheche."
Company 3	The company confirmed by telephone that it has not been sold. "We no longer belong to Fanhua, and we are not part of Cheche."
Company 4	The company had never heard of Cheche and confirmed by phone that their name is Fanhua and that would not change. "Life insurance is our main business."
Company 5	Phone interview 1: "Actually, we are the Fanhua sales team...We mostly sell life insurance." Phone interview 2: "I figure Cheche just wanted to use Fanhua's license to sell auto insurance. Our company is still Fanhua. There has been no acquisition, just a shift in selling auto insurance."
Company 6	"We have not sold insurance for more than a decade."
Company 7	"We've heard of the Cheche transaction, but what they do in management is unclear to us. . . . [this company] doesn't sell insurance anymore."
Company 8	We searched Baidu for the company and tried to locate anyone who had worked for the company but found nothing. No working phone number could be found.
Company 9	Interview 1: "We sell every type of insurance." Interview 2: "We still belong to Fanhua. We have not been sold."

January 17, 2019

Company 10	Interview 1: "Life, auto, P&C--we do everything. No special focus." Interview 2: "The auto insurance department is now managed by Cheche. Nothing else has changed."
Company 11	This company could not be found. We searched Baidu, government databases, and resume databases.
Company 12	"This company is going to be folded, and we will become a direct subsidiary of [Fanhua Group]." "But we're not supposed to talk about that."
Company 13	Interview 1: "We're an insurance agent; we sell every type of insurance." Interview 2: "Indeed, we are going to be sold to Cheche, but it's in process now."
Company 14	Interview 1: "Now we mostly sell life." Interview 2: "I've heard of Cheche but I'm not sure what they do."
Company 15	We found numbers using Baidu but no working phone number could be found.
Company 16	Interview 1: "We sell every type of insurance. We don't have a specialty." Interview 2: "We already belong to Cheche."
Company 17	Interview 1: "We sell life, auto, and P&C." Interview 2: "I don't know anything about a sale of the company."
Company 18	"We sell every type of insurance." Respondent would not answer questions about ownership.
Company 19	Would not respond to questions.

Source: List of company names in English from Fanhua 2017 20-F, Chinese language names and telephone interviews by J Capital.
We have anonymized the company names to protect the identities of people interviewed.

January 17, 2019

Appendix C:

Key Companies

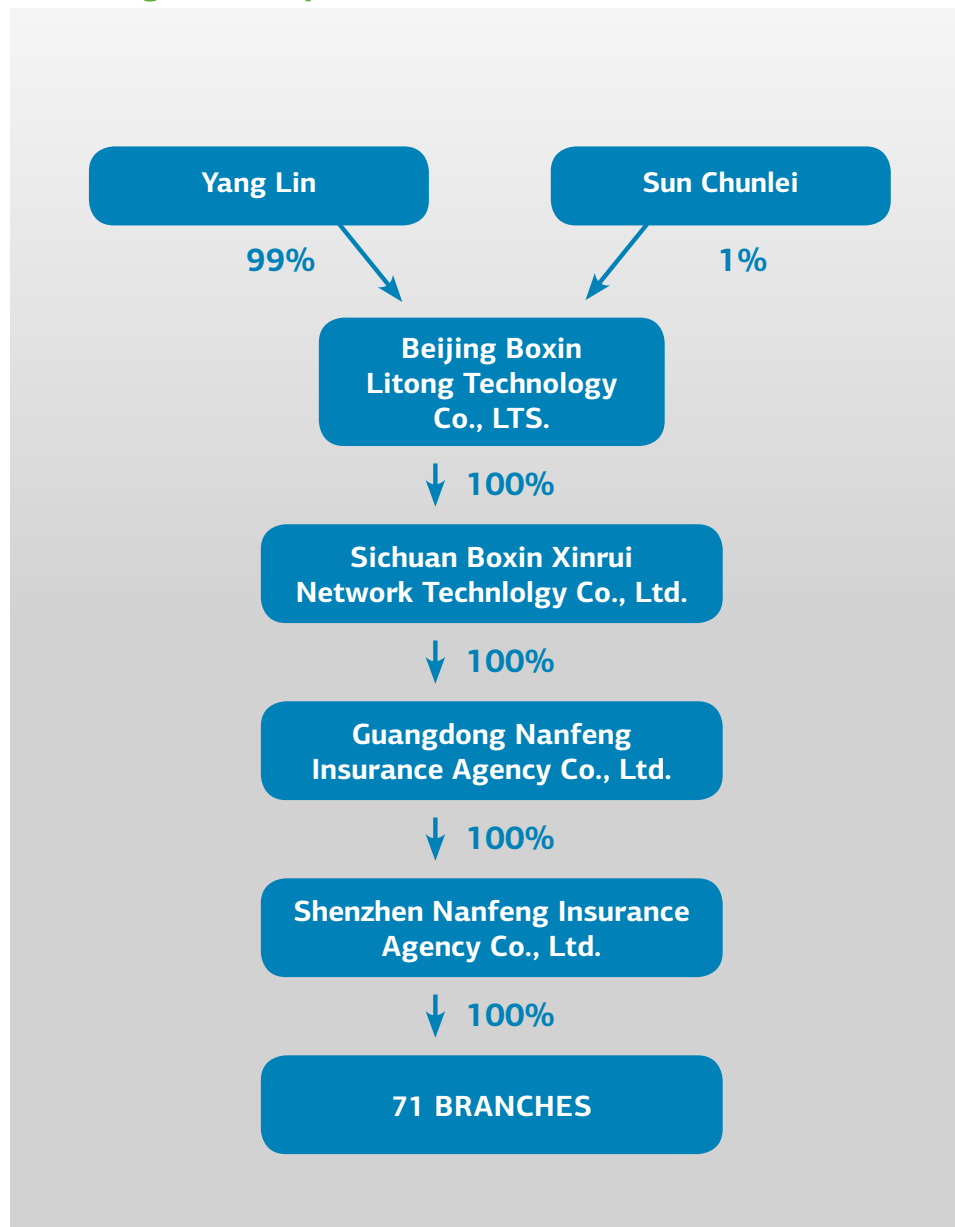
1. **Cheche:** Beijing Cheche Technology Co., Ltd., or Cheche, operates an online auto insurance platform. Fanhua reported that, in October 2017, it sold Cheche the equity interests in 19 P&C insurance intermediaries. Cheche is owned by three individuals and four companies. Cheche is controlled by its founder, Zhang Lei, who owns 33.58%.
2. **CNInsure:** The original name of Fanhua. Guangdong Nanfeng Enterprises, Guangzhou Nanyun Car Rental Services Co., Ltd., and Guangdong Nanfeng Automobile Association Co., Ltd. eventually became CNInsure, the predecessor of Fanhua. They were founded by Hu Yinan and Lai Qiuping from 1998 to 2001 to provide automobile-related services, such as car rental and emergency services. According to the company disclosures, in 1999, they began to sell automobile insurance products and automobile loans.

In 2009, Guangdong Nanfeng Automobile Association changed its name to Shenzhen Baolun Investment, which says that it engages in trade in diamonds, gold, platinum, and precious gems. Co-located with three wholly owned Fanhua companies, Baolun is also invested in three Fanhua companies.

3. **Fanhua Puyi Investment Management Co., Ltd.:** An agency selling investment products. Fanhua holds a 15.4% interest and Puyi manager Yu Haifeng's Chengdu Puyi Bohui Information Technology Co. Ltd. owns the balance. Several other companies called Puyi are also associated with Fanhua: Shanghai Puyi Investment Consulting Co. Ltd., Shanghai Puyi Asset Management Consulting, Shenzhen Puyi Zhongxiang Information Technology Co. Ltd., Renshou Puyi Company Management Center, and Xinzhiying Asset Management (Beijing) Co., Ltd., which is the new name of Puyi Asset Management (Beijing) Co. Ltd. These companies are controlled by Fanhua executives Yu Haifeng and Sun Conghai.
4. **The Yang Lin companies:** Sichuan Boxin Xinrui Network Technology Co. Ltd. and Beijing Boxin Lintong Information Technology Co. Ltd. are companies owned by Yang Lin, a Fanhua executive who frequently buys and sells equity from the company. Sichuan Boxin Xinrui is now the owner of most of the Fanhua Times companies that were reported sold to Cheche.

January 17, 2019

The Yang Lin Companies



5. **CNFinance Holdings (CNF):** Fanhua just IPO'd this division in November and retains a 20.58% stake. CNFinance extends and securitizes housing loans.
6. **The Target Companies:** Fanhua reported in its 2017 20-F that it had sold 19 companies to Beijing Cheche Technology. In fact, only six of the listed companies were actually sold to Cheche. The target companies are:
 - Beijing Fanlian Insurance Agency Co., Ltd.

January 17, 2019

- ▶ Beijing Fanhua Insurance Agency Co., Ltd.
- ▶ Beijing Fanhua Fumin Insurance Agency Co., Ltd.
- ▶ Tianjin Fanhua Xianghe Insurance Agency Co., Ltd.
- ▶ Hebei Fanlian Insurance Agency Co., Ltd.
- ▶ Shenyang Fangda Insurance Agency Co., Ltd.
- ▶ Nanjing Yukai Insurance Agency Co., Lt
- ▶ Hangzhou Fanhua Zhixin Insurance Agency Co., Ltd.
- ▶ Ninbo Baolian Insurance Agency Co., Ltd.
- ▶ Jiaxing Lianbao Insurance Agency Co., Ltd.
- ▶ Wenzhou Baolian Insurance Agency Co., Ltd.
- ▶ Henan Fanhua Anlian Insurance Agency Co., Ltd.
- ▶ Changsha Lianyi Insurance Agency Co., Ltd.
- ▶ Guangdong Nanfeng Insurance Agency Co., Ltd.
- ▶ Guangzhou Fanhua Yi'an Insurance Agency Co., Ltd.
- ▶ Dongguan Nanfeng Jiayu Insurance Agency Co., Ltd.
- ▶ Foshan Tuohua Insurance Agency Co., Ltd.
- ▶ Jiangmen Fanhua Zhicheng Insurance Agency Co., Ltd.
- ▶ Fanhua Kafusi Insurance Brokerage Co., Ltd.

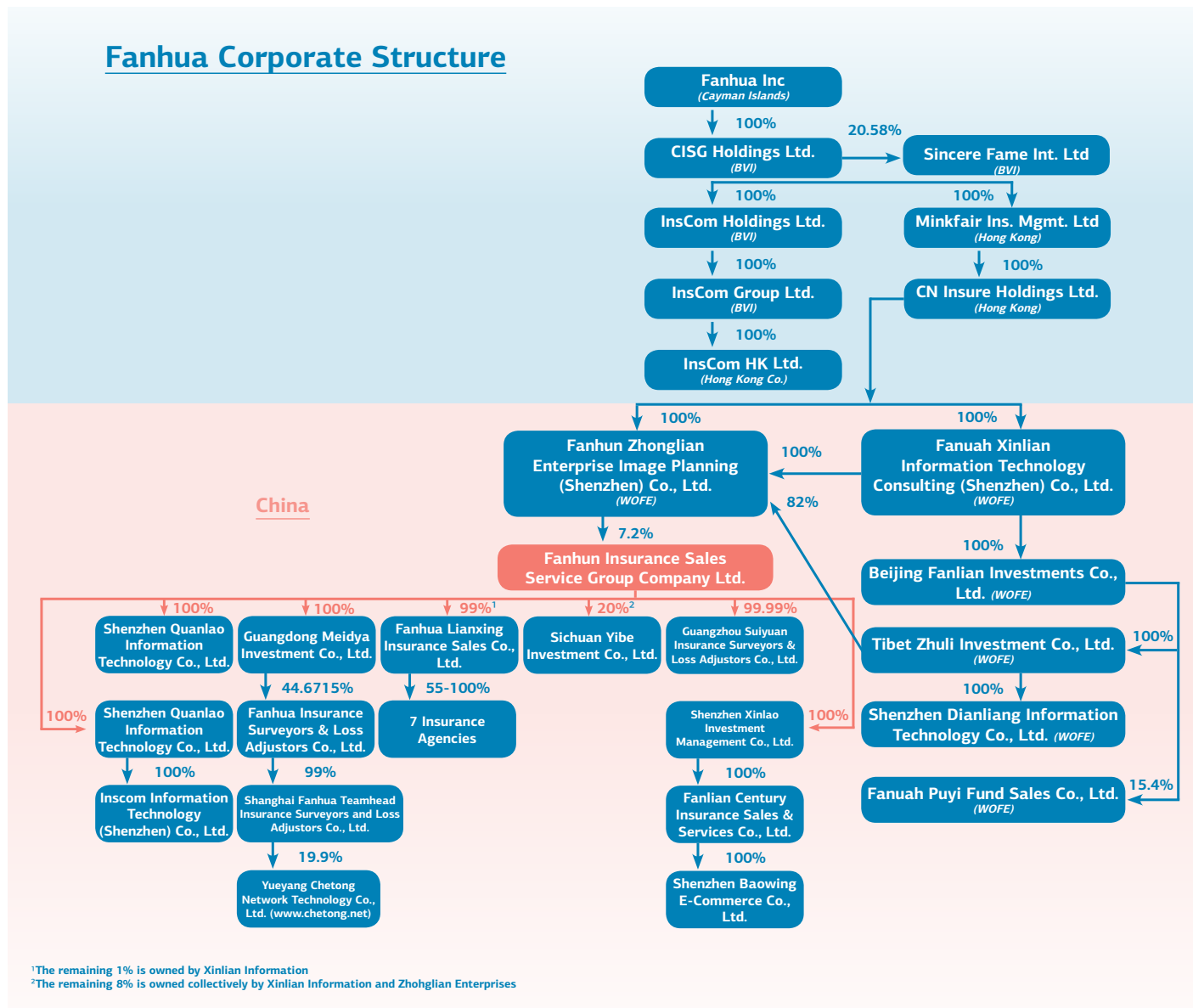
7. Beijing Ruisike Management Consulting Co., Ltd.: An indirectly held subsidiary established in 2007 and divested in 2017. The company reported that Ruisike was disposed of to a third party. “In January 2017, the Group disposed of Beijing Ruisike Management Consulting Co., Ltd to a third party, for a total cash consideration of RMB20,867, which was settled as of December 31, 2017. The Group recognized a gain of RMB2,029 on disposal of this subsidiary, which was determined by the excess of the sales consideration over the net book value of the subsidiary at the time of disposal.” (2017 20-F page F-28, filed April 20, 2018) But Ruisike was transferred to Liu Tingting, who identifies herself as Sales Manager for CNFinance. Our interviews confirmed that she is employed by Fanhua in Beijing.

8. Chengchuang (Shenzhen) Investment Co. Ltd.: A fund manager that manages trusts and private equity funds. Fanhua co-founder Lai Qiuping is the company owner. Fanhua sales agencies sell the Chengchuang financial products.

9. Guangzhou Huajie Insurance Agency: This company was identified in Fanhua’s 2014 20-F, filed April 24, 2015, as a 100% subsidiary of Fanhua’s and identified in a 13 G/A filed August 4, 2016 as a company wholly owned by Lai Qiuping. In the 2017 20-F, Fanhua reported dispos-

ing of Guangzhou Huajie. Chinese government records indicate that the company has always been owned by Lai Qiuping, although ownership has been shifted among holding companies belonging to him.

Chart 6. Fanhua Corporate Structure



Source: Company 2016 20-F page 46

January 17, 2019

Important FANH Bios

Cheng Huiqi

Cheng Huiqi was hired in 2008 as GM of Hunan Fanhua Insurance. Cheng received shares in Hunan Fanhua from Long Yubo's Tianjin Jingxu.



This 2008 notice from the China Insurance Regulatory Commission confirms that Chen Huiqi is general manager of Hunan Fanhua Insurance Agency.

Ge Peng

Chief financial officer since April 1, 2008, director since August 2007, and vice president since 2005. From 1994 to 1999, Mr. Ge was a financial manager at a subsidiary of China National Native Produce and Animal By-Products Import & Export Corporation. From 1999 to 2005, Ge headed the CNInsure Beijing operations. From 2005 to March 2008, Ge served as general manager of the finance and accounting department. He was named chief financial officer in 2008.

Hu Yinan

Co-founder of Fanhua with Lai Qiuping. With Lai, Hu formed two companies in Guangzhou to provide car rental and emergency services. In 1999, the companies began distributing automobile insurance and automobile loans. After obtaining capital from Cathay Capital Group, these companies became the foundation of CNInsure and, later, Fanhua. Hu resigned as CEO

January 17, 2019

of CNInsure in 2011 and as chairman in 2017.

Lai Qiuping

Lai Qiuping is a founder and former president of Fanhua and still owns 15.9% of the company. Fanhua recently paid Lai \$246.5 mln for shares he owned, saying they will redistribute the shares to executives and employees on completion of sales targets.

Since he retired from Fanhua, Lai has facilitated many of the investment businesses. Lai is owner of two Shenzhen-based companies that issue private equity securities sold by the Fanhua salesforce, Shenzhen CC Investment Co. Ltd. and Chengchuang (Shenzhen) Investment, and he has stakes in many more companies associated with Fanhua. Lai is a shareholder or executive of 56 current and former Fanhua-related companies within China, and that does not count his extensive offshore holdings.

Long Yubo

Deputy general manager of Puyi Wealth and owner of Tianjin Jingxu Investment Co. Ltd.



Sun Conghai

Sun was a university classmate of Hu Yinan's. A former professor of finance and founder of Puyi Fund Management, Sun is beneficial owner of Shanghai Puyi Investment Consulting, Shanghai Nanfeng Insurance Agency, Chengdu Puyi Bohui Infotech, and several other companies.

Sun Conghai | Photo: <http://www.pystandard.com/newsview.aspx?t=24&ContentId=7913>

Wang Chunlin

Fanhua director since 2016, chairman since 2017, CEO since 2011. Wang is director, executive, or owner of 37 companies. He was owner of Shenzhen Xinbao Investment Management, which Fanhua acquired in 2016.

Born in 1969, Wang joined Hu Yinan's auto-leasing company in 1998. He became Fanhua Insurance Group deputy general manager in 2007. In 2008, Wang became head of the assessment business under Fanhua. He was made CEO in 2011.

Yang Lin

[An article](#) that appeared in a Chinese publication called East Money de-

January 17, 2019

scribed Yang Lin as an executive who joined the Fanhua team in 2007. Our interviews with Fanhua employees were divided on his affiliation. One interviewee said Yang Lin was a Fanhua executive, but others said that he was “very close” to the company and to Fanhua CFO Ge Peng.

In June 2015, Fanhua also created a joint venture with a company that Yang Lin had established nine months earlier. The company was called Beijing Bopai Tongda. Fanhua has exited the company, but we have been unable to find any disclosures.

In 2014, according to Chinese corporate records, Yang Lin established Beijing Baoping Software as a technical platform for insurance sales. Barely one year later, Fanhua invested in the company and Fanhua CFO Ge Peng became chairman.

Yang Lin also owns three businesses based in the small Sichuan county where Fanhua founder Hu Yinan is from and where Fanhua is building a huge residential real estate project.

[Two published accounts](#) say that Yang Lin took over a Sichuan branch of Fanhua in 2015 and built it from 20 people to 1,626 in just two years, with comparable revenue growth.



Yu Haifeng | Photo from Sohu News, June 28, 2016

Yu Haifeng

Yu Haifeng is chief representative or majority owner of several asset management companies owned by Fanhua that generally go under the name Puyi. He also owns a company called Renshou Puyi Corporate Management Center in Renshou, Sichuan, where Fanhua is relocating its headquarters. [This article](#) says that Yu started Puyi on Fanhua's behalf. Three Fanhua employees confirmed to us that Yu is a Fanhua executive. Yu is also owner of Shenzhen Chuangji Investment Partnership, to which Fanhua extended loans in 2017 without disclosing them as loans to a related party.

Zhu Jiusheng

Fanhua executive and owner of Shanghai Miaofeng Investment.

January 17, 2019

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