Note: You should assume we have a short position in the securities of FMCN and China Lumena New Materials (067:HK) as of this report – prior to reading this report see important disclaimer on the last page before appendix (page 16).

Muddy Waters, LLC
Frauducation Part I: The Fraud School
April 10, 2012

Frauducation Part I: The Fraud School, RINO, and FSIN

Ever since Muddy Waters began writing about US-listed China frauds, we have been interested in learning more about the China-side networks that identify and dress up these companies for US listings. We have long viewed the China frauds as being products of organizations and networks, rather than numerous acts of lone company managements. A Chinese publication has just run an article that confirms there were sophisticated groups in China whose business has been to list frauds in the United States.

An April 3, 2012 article in Today's Fortune[1] called "Learning the Secrets of the Disaster of 'China Concept' Stocks" discusses an investigation into such a network, which the article dubs a "fraud school."[2] This fraud school was apparently involved in bringing our second fraud exposure target, RINO International Corp. (PINK: RINO), to the US market.

The article also identifies Fushi Copperweld, Inc. (NASDAQ: FSIN) as being among the companies that have worked with this fraud school. FSIN is currently the target of a troubled, non-binding takeover bid by its chairman. Because FSIN was an interesting case, we began looking at it internally early this year. Based on our early work on FSIN, we believe that it presents a high risk of fraud for a number of reasons, including its apparent association with the fraud school.

In this report, we discuss a) the fraud school article, b) a Hong Kong investment firm and auditor that was involved with RINO and FSIN, and c) why we believe FSIN presents a high risk of fraud. Note that we are not rating FSIN or any of the other stocks mentioned in this report.

<u>*Fraud School Investigation*</u>[3]

According to the article, the fraud school in question is a China-based investment firm that teaches businesses how to forge tax receipts, sales contracts, bank statements, government seals and official government documents. It also provides bookkeeping and accounting guidance designed to show companies how to cook their books. The school

[1] According to what a representative of Today's Fortune told us, it is a national finance and economics-oriented newspaper that publishes three editions per week and has a circulation of approximately 30,000.
[2] The original article and our in-house translation are in Appendix A
[3] This section summarizes the article. With the exception of our comments on the likelihood that it refers to Chief Capital, the contents of the section are restatements of the article.

and its consultants taught the companies how to keep the frauds going (and growing) once public.

The article states that the fraud school in question raised money for the following companies; however, the article does not state that these companies (with the exception of RINO) are frauds:

- FSIN, discussed in detail infra.
- RINO, which Muddy Waters exposed as a fraud in November 2010.
- American Lorain (AMEX: ALN, $45.2 million market cap, reported 2011 revenue of $213.2 million, trading at 0.3x book value and 2.3x P/E).
- Lihua International (NASDAQ: LIWA), which is a customer of FSIN.

The article states that the investigation into this fraud school began because the school worked with a Chinese manufacturer that raised pre-public funds from Chinese investors. Contrary to the plan, the manufacturer never went public in the US; and, its investors lost money and allege they were cheated. The authorities then began investigating this transaction and the fraud school. According to the article, the authorities are now in possession of two sets of records and financials for the manufacturer – one set forged, and the other set showing that it was losing substantial amounts of money. The forged documents were apparently based on templates that the fraud school provided.

How the Fraud School Makes Lemons into Lemonade[4]

The fraud school's assistance went well beyond providing document and accounting templates. The fraud school provided a network of "friendly" auditors that would help the companies get through the initial due diligence processes. The fraud school also helped companies game the due diligence process by providing the companies with contact information of suppliers and customers to give to potential investors. The suppliers and customers were frauds – the school hired them merely to play a role and answer questions according to the script.

Muddy Waters has long been aware that dishonest companies in China have played these games for years when Westerners have looked to source manufactured goods – commonly even borrowing a factory for purpose of giving tours to potential clients. We long ago ceased being shocked that companies would perpetrate such brazen frauds, and that there would be parties willing to assist (for a fee of course). Thus, Muddy Waters has always looked closely at companies' customers and suppliers. Typically, we approach these firms as potential customers ourselves, make site visits to them, and review their SAIC files.

The fraud school also arranged for its clients to prepare for investor site visits by renting inventory, temporary labor, and trucks. Fraud school companies were also taught that when they encountered the occasional investor who could figure out that the factory did

[4] This section summarizes the article with some editorial from MW.

not have the capacity to match the (forged) financials, the companies should respond that because business was so strong, they (the companies) were outsourcing to OEMs (original equipment manufacturers).

The web of the fraud school's lemonade factory includes law firms primarily based in the US. The American law firms are not under investigation in China, and it is unclear from the article whether the Chinese authorities suspect these law firms of knowingly helping to list frauds. Nonetheless, it is important for investors to be aware there may be law firms that fraud schools relied upon to bring troublesome listings to the US markets.

Once public, the companies would move up to larger auditors and law firms – particularly as they up-listed to the NASDAQ, AMEX, and NYSE. The larger accountants and law firms typically would bear the brunt of the blame in the US, even though the potentially more responsible parties were involved earlier in the process.

Chief Capital – a Hong Kong Investment Firm that Raised Money for RINO and FSIN

We looked for investment firms that were involved early with RINO and FSIN, and came across a Hong Kong investment firm called Chief Capital. Chief Capital's website states that it raised early funds for RINO and FSIN. Below is the deal list from the Chinese website:

Jimmy C.H. Cheung & Co. CPA – RINO and FSIN's First Auditor of Record

We knew of Jimmy C.H. Cheung & Co. CPA from our work on RINO. Cheung is a Hong Kong-based firm that was RINO's earliest auditor of record in SEC filings. Cheung also audited FSIN. Our research shows that Cheung audited the following Chinese RTOs:

- FSIN
- RINO
- ChinaCast Education Corp. (NASDAQ: CAST, previously the subject of negative research reports by OLP Global LLC (www.olpglobal.com) and Kerrisdale Capital Management, LLC (www.kerrisdalecap.com). CAST was halted on April 2, 2012 after the CEO was fired and allegedly withheld financial information that delayed the filing of company's 10-K, committed insider trading, and stole the company's seals, business licenses, and financial licenses.)
- China Northeast Petroleum Holdings Ltd. (AMEX: NEP, halted since March 1, 2012 due to an SEC investigation into possible fraud and possible misappropriation of $39 million)
- New Dragon Asia Corp. (PINK: NDAC, delisted from NYSE Amex on June 8, 2011)
- Northport Network Systems, Inc. (PINK: NNWS, delisted from OTCBB on April 5, 2010)
- Energroup Holdings Corp. (PINK: ENHD, filed Form 15 to terminate registration and suspend all future SEC filings on January 3, 2011)

FSIN – a High Risk of Fraud

We began looking at FSIN early this year because its bid appeared quite troubled – particularly in comparison to the management buyout of Harbin Electric that closed in November 2011. FSIN's chairman and two private equity firms have submitted a non-binding proposal to take FSIN private at $9.50 per share. The original bid was $11.50 per share, and was made in early November 2010.

We have found a number of problems with FSIN, and conclude that it presents a high risk of fraud. We are currently short FSIN as a result of our risk assessment.

We believe that FSIN presents a high risk of fraud for the following reasons:

- Factory surveillance and conversations with FSIN employees suggest that actual production volumes could be over 90% lower than FSIN's claimed sales.
- SAIC financials for the company that owns FSIN's Dalian Jinchuan facility suggest FSIN overstates that factory's revenue by as much as 7.4 times.
- Three of its key people have a history of involvement with troubled US listings of China companies.
- The SAIC financials for FSIN's largest production facility (approximately 70% of total revenue) roughly match the numbers FSIN reports in its SEC filings;

however, we found three categories of indicators that these SAIC financials could be forged. If these SAIC financials are in fact forged, then it begs the questions why FSIN would do so, and what the original financials showed.

- FSIN made two series of troubling asset purchases totaling $23.6 million. Chairman Fu was personally involved in these transactions in ways that make any arms length claim highly suspect. FSIN appears to have substantially overpaid for these assets – particularly for Dalian Jinchuan.

Site Investigations Indicate Far Lower Production Levels than Disclosed

We engaged professional investigators to perform over three days of surveillance of FSIN's main factory, and a tour of its secondary factory. In addition, the investigators spoke with FSIN employees at each location to learn more about production levels and the business.

FSIN's 2011 10-K states that FSIN sold approximately 29,000 tons of CCA and CCS from its primary factory in Dalian, China.[5] The combined dollar value of the revenue FSIN realized from its two China factories was $233.7 million.[6] FSIN attributes 86.5% of its China revenue ($202.1 million) to its Dalian Fushi factory (the "Fushi Plant") [7] at Number 1, Shuang Qiang Road, Yang Jia Village, Jinzhou District, Dalian.[8]

During three days of surveillance, the investigators observed very little materiel moving into or out of the factory. If the factory were producing and selling approximately 29,000 tons of CCA and CCS per year, we would expect to see five to 10 loaded heavy trucks in and out with materiel on an average day.[9] Instead, the investigators only saw two heavy truck movements the entire three days – shown below:

[5] FSIN 2011 10-K, p. 30.
[6] *Id*. at F-33.
[7] Calculated based on $233.7 million in total reported revenue from the China facilities per F-33 of the 2011 10-K, with 11% of the total revenue allocated to FSIN's Jinchuan subsidiary (per p. 15 of the 2011 10-K).
[8] FSIN 2011 10-K, p. 22.
[9] 29,000 tons / [250 – 350] days / maximum 25 tons per truck.

Alternatively, FSIN could be shipping via a much higher number of small trucks. However, during the three days of surveillance, the investigators noted only four small truck shipments in or out. This lack of activity is inconsistent with FSIN's reported production levels. Below are pictures of the each of the four other trucks the investigators observed:

The investigators spoke with a Fushi production line employee who had worked at the Fushi Plant for several years and painted a picture of actual production that is far lower than what FSIN's SEC filings claim. The employee stated that the factory has two production lines, each of which could produce three tons per shift. Each shift is eight hours. According to the employee, during the week (Monday through Friday), one line runs two shifts per day, and the other line runs one shift per day. He said that the plant is idle on the weekends. Assuming 50 production weeks per year, this yields only 2,250 tons of production, which is 92.2% lower than FSIN's reported 2011 production from this factory.

The investigator also visited FSIN's power cable factory, Dalian Jinchuan (the "Jinchuan Plant") at Maoyingzi Village, Dalian Bay Town, Ganjingzi District, Dalian (大连市甘井子区大连湾镇毛茔子村) . FSIN reported that this factory generated $29.1 million in 2011 revenue,[10] but our site visit and 2010 SAIC financials indicate that the real number is much lower. The investigator toured the plant on a weekday afternoon, and found the facility completely idle. The parking lot was virtually deserted. However, if FSIN's reported numbers are accurate, then based on 300 days of production per year,[11] the factory would on average produce approximately 15 tons per day.

[10] FSIN 2011 10-K, p. 29.
[11] This assumes an average of six working days per week, which is a fairly generous assumption for a company that is idle on a weekday afternoon.

Below are pictures of the factory taken during the weekday afternoon tour that show it idle:

The investigator met with a saleswoman who stated that the factory's peak production time is May through October, and during that time, the factory produces roughly 200 to 300 tons per month with an average per ton selling price of approximately RMB 40,000. The numbers from the saleswoman imply a ceiling revenue of $11.3 million for the six months (its peak period). However, because the factory seems significantly less busy the rest of the year, it is doubtful that using the saleswoman's estimates, the factory could have produced anywhere near $31.7 million in 2011 as FSIN claims.

The SAIC files for the entity that owns the Jinchuan Facility, Dalian Jinchuan Power Cable Co., Ltd. (大连金川电缆有限公司), show 2010 revenue of only $3.9 million, which is 86.6% less than FSIN reported. Note that the SAIC filing covers the entire year, while the SEC filing consolidates revenue only from February 5, 2010 onward, making the possible overstatement even larger. See below.

Dalian Jinchuan Power Cable Financial Results			
All Figures in Thousands	2009	2010	2011
SAIC: Revenue (RMB)	36,635	26,489	NA
SAIC: Revenue (USD[1])	5,363	3,913	NA
SAIC: Net Income (RMB)	481	354	NA
SAIC: Net Income (USD[1])	70	52	NA
SEC: Revenue[2,3] (USD)	NA	29,109	31,702
SEC: Net Income[2,3] (USD)	NA	4,298	NA
Revenue Overstatement	**NA**	**7.4x**	**NA**
Net Income Overstatement	**NA**	**12.1x**	**NA**

Note:

1 Revenue converted to USD using the average annual exchange rates provided for each year in FK's 10-K filings

2 Figures obtained through FSIN 2011 10-K, F-9 & F-31

2 2010 revenue and net income is noted in FSIN's filings as being for the period of February 5, 2010 through December 31, 2010

Key FSIN People Involved in Troubled China RTOs

As the article makes clear, the people involved in a company can be an important indicator of corporate wrongdoing – particularly if they seem to have a pattern of involvement in troublesome companies. This is not to say that these people are complicit in fraud, wrongdoing, or knowingly become involved with low quality companies. However, having individuals who have been involved with multiple problem companies is a risk factor that investors should consider.

FSIN currently has three individuals who serve as officers or directors who are, or have been, involved with a number of questionable US-listed China RTOs. The companies linked to FSIN by virtue of these individuals are:

- CBEH (PINK), China Integrated Energy, Inc., which was halted in April 2011 and subsequently delisted from NASDAQ on June 15, 2011. It had been the subject of fraud allegations by Alfred Little (www.alfredlittle.com).
- CGA (NYSE), China Green Agriculture. It had been the subject of negative research reports by IFRA (www.ifragroup.com) and J Capital Research (www.jcapitalresearch.com).
- ENHD (PINK), Energroup Holdings Corp., which was delisted from OTCBB and filed Form 15 to terminate its registration and suspend all securities filings on January 3, 2011.
- GSI (NYSE), General Steel Holdings, Inc.
- Harbin Electric, which was acquired by a group led by its chairman at $24 per share. Prior to the acquisition, it had been the subject of negative research reports by Citron Research (www.citronresearch.com).
- NEP (AMEX), China Northeast Petroleum Holdings, Inc., which has been halted since March 1, 2012.
- ONP (AMEX), Orient Paper, Inc. ONP was the subject of Muddy Waters's first fraud report.
- SGTI (OTCBB), Shengtai Pharmaceutical, Inc., which has a market capitalization of $9.6 million on reported 2011 revenue of $171.7 million, trading at 0.16x book value and 2.3x P/E.
- SHZ (AMEX), China Shenzhou Mining & Resources, Inc., which was the subject of negative a research report by Absaroka Capital Management, LLC (www.absaroka.com).

The SAIC Financials for Fushi Dalian Support Reported Sales Numbers; However, We Have Concerns About the Integrity of these Financials

In the early days of exposing US-listed China frauds (roughly 2010), we believed that SAIC financials, which often greatly contradicted the numbers companies reported to the SEC, were a valuable indicator of companies' true business volumes. When we researched Duoyuan Global Water (previously DGW, now DGWIY) in February and March 2011, we caught DGWIY red-handed in substituting forged audit reports (supporting its reported revenue) for authentic reports (showing a fraction of reported revenue). This confirmed a) that US-listed companies had become aware that investors were looking at their SAIC financials for confirmation, and b) there were channels to replace genuine SAIC files with forged ones.

We have found three categories of indicators that the SAIC financials for the entity owning the Fushi Plant are not original or authentic. The documents in question are audit reports prepared by PRC-licensed accounting firms. The issues we have identified with the documents (the important pages of which are provided in Appendix C) are:

- The 2008 and 2010 financial statements are missing the company's seal ("chop").
- The 2010 financial statements are missing the auditor's chop and the accountant's seals.

- The formatting in parts of the 2009 audit report appears unusually unprofessional.

Ironically FSIN's recently-filed 2011 10-K contains the following risk disclosure:

> The financial information contained in the Company's PRC subsidiaries' filings with the State Administration for Industry and Commerce (SAIC) are consistent with the financial information contained in the Company's SEC filing. However, the Company believes there may be fabricated SAIC reports which may be used by the short sellers to attack the Company.[12]

FSIN's Suspicious Asset Purchases that Present Risks of Fraud and Theft

FSIN purchased two sets of assets in manners that raise red flags regarding whether the prices paid were too high. These transactions are the 2010 $10.2 million purchase of the company that owns the Jinchuan Plant, which seems particularly high; and, the 2010 $13.4 million purchase of assets belonging to a bimetallic wire producer named Shanghai Hongtai ("Hongtai") and land use rights for relocation of the assets.

In January 2010, FSIN purchased the company that owns the Jinchuan Plant for $10.15 million (RMB 69.3 million), Dalian Jinchuan Cable Co. Ltd. (the "Jinchuan Co"). We have four issues with this purchase. First, our previously discussed observations of FSIN's primary China factory, the Fushi Plant, make any capacity expansion questionable. Second, and just as troubling, FSIN's chairman and controlling shareholder, Li Fu, previously controlled the Jinchuan Co. Third, FSIN has misled investors about the process by which ownership of the Jinchuan Co passed to Chairman Fu (and then to FSIN). Finally, we believe that FSIN substantially overpaid for the company ($10.2 million purchase consideration) based on our observation that there is no production occurring, its 2010 SAIC reported revenue of $3.9 million (86.6% lower than SEC filings), and its $1.6 million registered capital, and then $2.2 million of shareholders' equity.

Significantly, FSIN misled investors about how Chairman Fu came to control the Jinchuan Co. Chairman Fu and a senior FSIN employee, Chunyan Xu, acquired 100% of the Jinchuan Co in March 2008, with Chairman Fu owning 78.4% of the company and Ms. Xu holding the remainder. FSIN disclosed Chairman Fu's prior ownership, but stated that the transfer of Jinchuan Co shares to Chairman Fu and Ms. Xu was to secure a RMB 15 million personal loan Chairman Fu had made to the selling shareholders of the Jinchuan Co.

<u>The problem is that the shareholders who transferred the Jinchuan Co to Chairman Fu (i.e., the selling shareholders) are different than the ones who received it from him for the short period of time before FSIN acquired it. Therefore, FSIN lied to shareholders about this series of transactions, seriously calling into question whether they were truly arms-length</u>.

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[12] FSIN 2011 10-K, p. 14.

The table below shows the various shareholders of the Jinchuan Co.

Date	Shareholders	Ownership %	Capital Contribution (RMB'000)	Legal Representative & Supervisor	Registered Capital (RMB'000)
April 2007	Yu Ju	61%	6,805	Legal Representative: Yu Ju	11,129
	Yan Ju	22%	2,400	Supervisor: Xueqin Zhang	
	Xueqin Zhang	17%	1,923		
27-Mar-08	Li Fu	78%	8,729	Legal Representative: Chunyan Xu	11,129
	Chunyan Xu	22%	2,400	Supervisor: Li Fu	
14-Dec-09	Binchang Liang	78%	8,729	Legal Representative: Chunyan Xu	11,129
	Luyuan Liu	22%	2,400	Supervisor: Li Fu	
6-Jan-10	Binchang Liang	78%	8,729	Legal Representative: Binchang Liang	11,129
	Luyuan Liu	22%	2,400	Supervisor: Li Fu	
1-Mar-10	Binchang Liang	78%	8,729	Legal Representative: Chunyan Xu	11,129
	Luyuan Liu	22%	2,400	Supervisor: Li Fu	
17-Mar-10	Fushi International (Dalian) Bimetallic Cable Co., Ltd.	100%	11,129	Legal Representative: Chunyan Xu Supervisor: Li Fu	11,129

According to FSIN, Mr. Fu during this time had no shareholder rights (e.g., dividends, voting) in the company, nor did he have any obligation to absorb or finance the Jinchaun Co's losses.[13]

In December 2009, Chairman Fu and Ms. Xu transferred the Jinchuan Co. to two individuals, who maintained the same ownership percentages. Significantly, Mr. Xu remained the Jinchuan Co's Legal Representative, and Chairman Fu remained its Supervisor. This could indicate that the two, although surrendering legal title, effectively remained in control of the Jinchuan Co.

In January 2010 – two months prior to selling the Jinchuan Co to FSIN, the Legal Representative changed from Ms. Xu to the then-majority shareholder. One wonders what legitimate benefit could have been achieved by changing the Legal Representative just prior to the sale – particularly when the individual who surrendered the position would again become the Legal Representative just two months later. Rather, the 11th hour change could have been an attempt to make the impending sale to FSIN appear to be arms length.

In January 2010, FSIN acquired the Jinchuan Co for $10.2 million. The registered capital (i.e., paid-in equity capital) of the Jinchuan Co was only $1.6 million at the time (somewhat consistent with a RMB 15 million loan). The total assets were only $4.0 million and the shareholders' equity was only $2.2 million. Given that the purchase payment was 6.3 times the registered capital and 5.7 times December 31, 2009 book value, and the Jinchuan Co is a manufacturer (meaning that there is a strong correlation between the registered capital and the company's economic value), we believe that FSIN significantly overpaid for the acquisition.

[13] FSIN 2011 10-K, F-31.

On May 27, 2010 FSIN agreed to purchase substantially all of the assets of Shanghai Hongtai Industrial Co. Ltd. ("Hongtai"), which is a bimetallic wire producer for $3.9 million.[14] The assets are to be used by a FSIN subsidiary established in 2010 in Jiangsu province ("Fushi Jiangsu"), so the Hongtai transaction appears to be the raison d'être for Fushi Jiangsu.

We have four concerns about this series of transactions. First, it appears that FSIN provided the funds for Chairman Fu to personally own Hongtai, which FSIN states generated approximately $10 million in annual revenue prior to the transaction. Second, the funding structure for Fushi Jiangsu is unusual and raises questions of conflict of interest. Third, the purchase appears to add superfluous capacity. Fourth, we believe that the $9.5 million land use rights prepayment in Yixing, Jiangsu for the Hongtai assets needs further disclosure – particularly because FSIN has not received the rights[15] despite paying one year earlier.

FSIN made the following disclosure about the Hongtai purchase, which appears to mean that Chairman Fu used company funds to become the shareholder of Hongtai:

> On May 31, 2010 ("the acquisition-date"), Fushi International completed the acquisition of Hongtai by designating the Company's Co-Chief Executive Officer ("Co-CEO") Li Fu to acquire Hongtai as the Company's legal representative during this transitional period of Fushi Jiangsu as described above. Mr. Li Fu is currently appointed as the sole member of Hongtai's board. Such duties carried out by the Company's Co-CEO did not result in additional compensation provided to the Co-CEO. In addition, the Company funded all such considerations as described below related to the acquisition of Hongtai.[16]

If our interpretation of the above passage is correct, and Chairman Fu became the shareholder of Hongtai, it is a very negative sign for FSIN's internal controls and corporate governance.

Fushi Jiangsu was funded by $23.0 million in USD loans made in September and October 2010 by Chairman Fu.[17] FSIN immediately repaid the loans by RMB transfer to Chairman Fu.[18] When amounts of money this large flow between the controlling shareholder and the company, there is a substantial conflict of interest and potential for abuse.

Fushi Jiangsu appears to be an unnecessary addition to FSIN's capacity based on our investigator's observations in Dalian. Bolstering that view is the fact that as of December 31, 2011, it had not begun production.[19] What makes the Hongtai acquisition even more

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[14] FSIN 2011 10-K, F-31. The purchase consideration consists of $1.3 million cash, and $2.6 million of FSIN shares.
[15] As of the date of the 2011 10-K.
[16] FSIN Q2 2010 10-Q, p. 26.
[17] FSIN 2011 10-K, F-34.
[18] *Id*.
[19] FSIN 2011 10-K, F-32.

quixotic is that Hongtai, which FSIN states was generating approximately $10 million in annual revenue,[20] would seem to have been idle for over 20 months since the acquisition. FSIN stated that it intended to relocate key personnel from Hongtai to (idle) Yixing.[21] What are those key personnel currently doing?

FSIN prepaid $9.5 million for land use rights in Yixing for Fushi Jiangsu in December 2010; however, as of March 15, 2012, the rights had not been granted to FSIN. To the extent that Fushi Jiangsu will be limited to using the Hongtai assets, the land transaction seems substantial relative to the production size of Hongtai (at roughly $10 million annual revenue). FSIN seems that granted industrial land use rights in Yixing sell for approximately $55 per square meter. Our ballpark estimate is therefore that FSIN is acquiring 172,000 square meters of land. It seems to have China factories with a plot ratio of roughly 0.65. If it used the same plot ratio, then it would imply a facility of 112,000 square meters. This would be FSIN's largest factory in China by area.

We are not encouraged by the scant disclosure of information related to this transaction; specifically we would like to know:

- the size of the parcel,
- the address of the parcel,
- the payee of the $9.5 million,
- the to-be grantor of the parcel,
- the term of the land use rights, including the remaining term,
- the reason for delay in issuing the rights,
- specifications of the facility FSIN plans for the parcel,

The amounts of money involved in these transactions are large, and due to the lack of disclosures and Chairman Fu's personal involvement in these transactions, they are a clear red flag regarding investing in FSIN.

Chairman Fu's Troubled Bid for FSIN

Questions about FSIN's fraud risk are less relevant than questions about the risk of Chairman Fu's failure to take FSIN private. Logically if FSIN were committing material fraud, then it would not behoove Chairman Fu to buy it at a premium to its current share price. Regardless of whether FSIN is a fraud, we note that the bid has a troubled history, which does not bode will for his ability to close the transaction.

On November 3, 2010, Chairman Fu submitted by letter his initial bid to purchase the 70.8% of FSIN that he did not hold for $11.50 per share. The stock had previously closed at $9.10. The buyout proposal called for a private equity firm, Abax Global Capital (Hong Kong) Ltd. to also participate. In reaction to the buyout proposal,

[20] FSIN 8-K, filed May 27, 2010.
[21] *Id*.

shareholders filed class action suits against FSIN alleging that the consideration was too low.

On March 1, 2011, FSIN announced that a special committee of its board, formed to evaluate the MBO proposal, had hired Bank of America Merrill Lynch and a law firm to advise it. It is interesting that the company took such a long time to find advisors for this transaction.

On May 26, 2011, FSIN announced that its special committee was "facilitating" due diligence by Chairman Fu and Abax.

On November 21, 2011, FSIN announced that Chairman Fu and Abax lowered their bid to $9.25 per share. FSIN noted in the announcement that the new proposal "does not contain customary financing commitments and is still highly conditional."[22] On December 28, 2011, FSIN announced that Chairman Fu and Abax raised their bid to $9.50 per share, but that the bid still did not contain financing commitments and was still highly conditional. The new proposal includes TPG Growth Asia, Inc. as an equity sponsor, and states that China Development Bank will provide debt financing.

We note that Harbin Electric's Chairman Yang announced his take private bid on October 11, 2010, and it closed on November 3, 2011. Despite significant volatility in the stock price during that time, Chairman Yang closed the transaction at the initially announced price: $24 per share. Although the Harbin Electric MBO was not entirely smooth, the amount of time it is taking Chairman Fu to close and his changing bid prices are an interesting contrast.

[22] FSIN 8-K, filed November 21, 2011.

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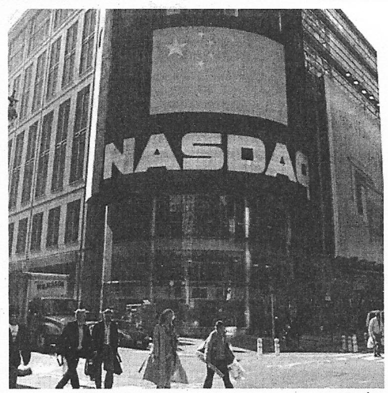
来自美国本报特稿

中国概念股灾揭秘

■ 约翰 凯恩斯(John Caines)

投融资圈内人士皆知,近两年来在美国上市的中国公司,遭遇了全面的信誉危机。中国概念股被投资人疯狂抛售,股价大跌,几乎全军覆没。但很少人知道,酿成这一股灾幕后的真正原因:一小撮专业金融诈骗高手破坏了大多数中国企业在美国股市的商业信誉,并酿成了危机。



据几家上当受骗的美国投资人透露,中国警方正在积极介入调查一个十分老练的"金融诈骗学校"有系统地制造虚假中国企业赴美上市的案例。这一诈骗学校通过他们成熟的操作系统教授那些急功近利的中国企业如何伪造销售合同、政府文件、并操纵其财务报表,以达到在美国 OTCBB,NASDAQ,AMEX 和 NYSE 上市套钱目的。

据透露,该"金融欺诈学校"是一家小型的投资银行和金融顾问公司。它利用其在香港和美国的会计事务所和律师事务所关系网络进行专业分工,联合运作,把一些"垃圾"企业包装成快速成长和巨大盈利的超级巨星,以骗取外国投资者的青睐,进行私募融资,然后在美上市。目前案子调查的重点是这家小型投行和其包装的一家中国民营制造业公司,本打算去美国上市,但未果。由于本案的刑事和民事诉讼案正在进行中,有关部门目前不便透露被调查投行和企业的名称,但官方手中已经掌握了涉嫌企业的原始财务凭证和虚假的财务报告及相关材料。这些文件清楚表明这家公司实际经营连年严重亏本,但"金融诈骗学校"却向投资人出具了特别诱人的业绩报告,并有正式的财务审计报告支持,骗取了投资人数百万美金的过桥投资。但由于劣迹暴露,后期融资流产。

虽然,目前调查围绕着该小型投行进行,但并不排除调查可能延伸至相关会计事务所及"金融诈骗学校"系统其他成员。由此,投资人有理由怀疑这家小型投行和其合作的会计及律师事务所参与过的其他公司的真实性。据透露,他们所参与在美上市运作的公司包括 Fushi Copperweld (NASDAQ:FSIN),Lihua International (NASDAQ:LIWA),American Lorain (AMEX:ALN),Dalian RINO International(OTN:RINO)。目前的调查主要在中国境内进行,还未涉及到相关的承接中国公司在美上市业务的律师事务所。

据了解,这家"金融诈骗学校"(小型投行公司)进行欺诈典型的做法是,通过他们所谓投融资顾问网络寻找愿配合的中小企业进行培训和伪包装。第一步,通过反向收购将其推上美国 OTCBB 市场。然后,继续辅导公司制造各类相关上报文件和伪造数据,使其不断膨胀,以便转到主板上市,进行套现。"金融诈骗学校"可以向其所包装的对象企业提供美国会计准则审计报表数据模板,并教导他们如何操作个别会计行项目产生显著的营业额、利润和现金余额。"金融诈骗学校"并教导对象企业如何准备虚假财务数据、税收票据、银行对账单和销售合同。为了让超级巨星的故事更可信,他们可向投资人提供事先准备好的所谓客户名单和电话号码等信息,以备供投资人查证。当投资人实地考察公司生产和经营状况时,骗子们会马上雇用临时工人,摆上生产样品,租来库存和集装箱卡车,为投资人演一场热火朝天的生产和出货的好戏。当投资人发现工厂的生产线即使满负荷运转,也远远不能产生财务数据上的漂亮营业额时,他们会谎称订单太多,接不过来,已经外包给外地其它工厂代加工生产……最后,该小型投行与他们长期合作的会计审计所沟通,以确保这些伪造材料顺利通过其审计,并为对象企业出具正式完美无缺的审计报告。并确保这些审计报告在那些权威专家眼中也显得非常可信。根据本案律师手中所掌握的伪造财务报表、发票、银行对账单和有关部门公章等一系列材料来看,该案子揭示了一个有组织有系统的作案平台,它甚至能欺骗和蒙蔽经验丰富的投资人和美国证监会。

通常情况下,当"金融诈骗学校"培训的对象公司从 OTCBB 成功转版到主板股票交易市场后,前期的咨询顾问公司、会计审计所、律师事务所将被美国当地更大的,更有信誉的投行、审计和律师事务所接替,从而吸引更大的投资者和较大的投资金额。当投资人最后发现被欺诈时,往往会将这些罪过归咎于这些美国当地信誉良好的财会审计所和律师事务所和他们代表的中国企业。殊不知,原始的罪魁祸首——"金融诈骗学校"这时已经金蝉脱壳,溜之大吉,坐收渔翁之利。这是美国投资人根本无从得知的幕后背景。

举个真实典型的例子,在纳斯达克上市的大连绿诺(RINO)是"金融诈骗学校"的早期毕业生。该公司于 2010 年 11 月被发现有严重的财务欺诈行为,最终被摘牌。投资人遭受了近 8 亿美元的损失。美国证监会调查了在美直接为其服务的投行、会计所、律师所,并严厉追究这些大机构的责任。但鲜为人知的是,这一金融诈骗的种子早在数年前就被"金融诈骗学校"埋下了,后面只是到美国生根发芽并结果而已。美国当地的投行、会计所、律师所只是替罪羊。据透露,由于同一圈子的人曾参与 FUSHI 在美私募及上市工作,尽管目前没有直接证据表明 FUSHI 有问题,但市场上对 FUSHI 公司的怀疑气氛仍然存在。据业界有关人士称,FUSHI 公司目前正准备摘牌下市。由此,一些市场分析家认为 FUSHI 的这一动议可能与他们想规避美国市场、股民及证监会对其监察有关。这一判断的依据是,2011 年 FUSHI 公司在一集体诉讼案中被指控捏造财务数据,误导投资人。美国福布斯杂志同年报道了包括 FUSHI 公司在内的大量的舞弊指控诉讼案件,并把这类案件比喻为"中国版的安然和世界通信公司"。

在大连绿诺事件后,美国国会高度重视中国企业在美上市财务欺诈问题,并开展了对代表这些中国企业的美国投行、财务顾问公司、财务审计所和律师所一番详尽调查。但没有人触及那些在中国发起了这些欺诈案子的诈骗学校。受害公司之一 Fair City 的张小姐(Angela Zhang)说:"在过去,一般是外国人受了骗赔了钱。但这案子中,受了骗赔了钱的人不仅是老外。目前的调查,证明了中国有关部门对此类案子的高度重视,正如美国政府在美国追究那些当事人一样"。作为这一案子的领衔律师,杨律师代表上当受骗的投资人向涉嫌欺诈企业、投行、审计所追索经济赔偿。杨律师说:"目前官方对诈骗学校严肃的调查将会对恢复中国企业在投资人中,尤其是在外国投资人中的信誉起到十分积极有力的作用"。

根据美国官方统计数据,一些中国在美上市企业的财务欺诈问题使投资人在过去 5 年中损失了近 350 亿美金,并对中国在海外金融市场的形象和信誉产生了极为负面的影响。正可谓一条臭鱼腥一锅汤,这些少数的造假企业殃及了整个美国市场上中国概念股,使许多良好的上市公司也遭遇了不应得的损失。在美国,这一"中国概念股冬天"的后果将需要数年才能够等到修复。

《2012 中国高净值人群消费需求白皮书》发布——

中国 270 万人资产超 600 万

旅游和养生最受他们关注;13%亿万富豪有意购买公务机

■ 记者 李颖

2011 年 10 月至 2012 年 1 月间,兴业银行与胡润研究院面对面地访问了几十位私人银行客户,并对全国 29 个城市的个人资产在 600 万元以上的高净值人群进行了问卷调查,共获得 878 份有效问卷。他们的平均财富达到 4900 万人民币以上,平均年消费为 145 万,占平均财富的 3%。平均年龄为 39 岁。

目前,中国高净值人群已达到 270 万人。其中,亿万资产以上的高净值人群数量约 6.35 万人,平均年龄为 41 岁……

中国到底有多少富豪?他们最关注什么?他们投资于哪些领域?日前,随着《2012 中国高净值人群消费需求白皮书》的发布,这些答案都已揭晓。

亿万富豪送礼最爱送红酒

亿万资产以上的高净值人群每年的赠礼花费约 15 万,占平均年消费的 10%,其中 8 成用在商务场合,超过 4 成高净值人群需要在婚礼和节庆场合赠送礼品。

而从礼品来看,手表是高净值人群最常赠送给男士的礼物,不过在亿万资产以上的高净值人群中,红酒是最常见的礼品。

同时,公务机对高净值人群有很大的吸引力,13%亿万富豪有意购买公务机。

最关注旅游、养生、子女教育

旅游、养生保健、子女教育是最近高净值人群最期待私人银行提供的增值服务。

高净值人群最希望得到金融服务的消费领域是旅游,有 6 成高净值人群表示会选择旅游方面的消费金融服务。此外,半数高净值人群青睐养生保健方面的服务,超过 1/3 的高净值人群选择子女教育类的服务。85%的高净值人群有计划送孩子出国留学,亿万富豪中达到 90%。46%的高净值人群对子女的教育理念是全面发展,41%是素质能力教育,23%是创造性教育,17%是开放性教育,14%是个性化教育。

对于自己,7 成富豪愿意再次参加高级培训课程,人脉对他们最重要;阅读、参加各种论坛讲座、进修班和培训课程是高净值人群提升自我的方式。

同时,人脉对他们最重要。

富豪最热衷收藏手表

6 成以上的高净值人群有收藏的习惯,平均收藏的时间超过 4 年,也就是说大约从 2008 年开始收藏。其中,7 成以上亿万资产以上的高净值人群有收藏习惯,平均收藏的时间为 5.6 年,也就是说亿万富豪大约从 2006 年开始收藏。高净值人群的收藏选择多种多样,最热衷于收藏手表,也有部分高净值人群会选择艺术品,如古代字画、瓷杂和当代艺术品。

■分析

中国富豪进入守富阶段

中国高净值人群生活方式主要分为三个阶段:创富、守富和享富阶段。中国高净值人群经历了利用奢侈品品牌凸显社会地位的创富阶段,已步入以低调、适用型的生活方式为主的守富阶段,并逐步向以投身公益慈善事业为代表的享富阶段过渡。

其中守富阶段的主要特征为:适度消费,开始注重生活的品质、自身的身心修养及子女的内涵气质教育。

在守富阶段,高净值人士常常参加各种私人会所,尝试高尔夫、马术等高端运动,积极参加总裁培训班等课程,在业余时间品酒、品茶或是与有同样收藏爱好的人士交流,这使得消费成为高净值人群联系的纽带和沟通的平台。净值人群通过消费扩大自己的社交范围,与朋友交流,形成一个个以财富为基础的"社交圈"。胡润百富创始人兼首席调研员胡润说:"虽然中国富豪的消费能力很大,但现在我感觉他们还在从富豪到新贵族转变的路上。"

■调查

九成富豪拟送子女出国 65%网友表示理解富豪们的决定

名为"中国九成亿万富豪拟送子女出国留学,你怎么看"的网络调查,大约有超过两万名网友参与了调查。结果显示,大多数网友理解富豪们的决定,并对中国目前的教育质量表示了担忧,选择"理解,对国内教改失望和对国内教育理念不认同,出国留学成为必然"的网友共有 16930 名,占全部投票网友中的 65.34%;选择"支持,能让孩子开拓眼界花再多钱都值"的有 3241 人,占 12.51%;选择"反对,无非是跟风行为,外国的月亮不一定圆"的只有 1885 人,仅占 7.28%;剩下的网友表示不关心,"只要花的不是纳税人的钱"。

对于这个话题,大部分参与调查的网友都表示了对国内教育制度和质量的担忧,微博网友 @ 汐汐之家就调侃说:"在国外不用遇到奇奇怪怪的老师,没有奇奇怪怪的环境,更没有奇奇怪怪的食品,不用坐奇奇怪怪的校车。"而微博网友 @ 静雅则担忧,留学之门对富豪敞开更挤压了穷人后代的空间:"一些有专业特长的孩子,一些各方面都比较均衡优良的孩子得不到好的教育,无法进入自己希望的、更高的学府求学,有钱的选择出国,而没钱的呢?"

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Article Translation

Learning the Secrets of the Disaster of "China Concept" Stocks

By John Caines

Wall Street insiders all know that Chinese companies listed in the US have been encountering a full-scale credibility crisis for the recent two years. There has been a wave of selling "China Concept" stocks among investors, and the stock prices have fallen down sharply, and nearly all of the China Concept stocks are tanking. But few people know that the real reason behind the curtain of the disaster is a handful of financial fraud professionals who have destroyed the credit of most Chinese enterprises listed in the US stock market and caused the current crisis.

According to several US investors who were cheated, the Chinese police are actively investigating a case regarding systematically taking fake Chinese enterprises public in the US by a very sophisticated "fraud school". This fraud school teaches those Chinese enterprises which are eager for quick profit through their sophisticate mechanism how to make fake sales contracts, fake government filings, and manipulate financial statements to achieve the goal of collecting money by being listed on OTCBB, NASDAQ, AMEX and/or the NYSE.

According to a source, the "fraud school" is a small investment bank and financing counseling company. It uses a network of accounting firms and law firms based in HK and US to jointly operate to present "trash" enterprises as fast-growing and huge-profit-making super stars, thus catching the foreign investors' eyes, gaining private funding, and subsequently going public in the US. Now the investigation is focused on this small investment bank and a Chinese private-owned manufacturer educated and polished by it which intended to go public in the US, but was unable to. The relevant authorities believe it is inappropriate to reveal the name of the investment bank and the enterprise because the relevant criminal and civil proceedings are currently in progress but authorities have already obtained the company's real financial documents, its falsified financial documents, and other relevant materials. The firm's true documents clearly indicated that the actual operation of this company have suffered losses for several consecutive years, but the "fraud school" showed a very attractive financial figures to the investors, supported by formal financial reports, and thus cheated the investors out of millions of dollars in bridge loans. Due to the exposure of the fraud school and its client, a financing round that would have otherwise gone through was aborted.

Even if the current investigation is limited to this small investment bank, it does not preclude the possibility that it will extend to the relevant accountant firm and other members of the "fraud schools". Investors have reason to doubt the authenticity of the small investment bank, and those companies which had been served by its cooperating accountant and the law firm. According to a source, companies that went public in the US through the services of this investment bank and its cooperating accountants and law firms include Fushi Copperweld (NASDAQ: FSIN), Lihua International (NASDAQ: LIWA), American Lorain (AMEX: ALN), Dalian RINO International (PINK: RINO). Now the investigation is carried out mainly within China, it has not spread to the Law Firms which were engaged in the going public service for those companies.

This “fraud school” has a standard way to conduct fraud. It looks for small to medium-sized enterprises through a so-called “investment-financing counsel network”, provides training and forgery assistance. During the first step, they will put help a company go public on the US OTCBB through reverse merger. After that, they will keep coaching the firm on producing falsified reporting documents in order to make it keep “growing” with the eventual goal of listing on a primary exchange (i.e. NYSE or NASDAQ) and collect even more money from US investors. The “fraud school” may provides data templates of financing sheets in accordance with the US accounting rules, and coach them how to manipulate the specific accounting line item to make out prominent revenue, profit and balance of cash. The “fraud school” also coaches its client companies on how to prepare fake financial figures, tax receipts, bank statements and sales contracts. To make the “super star” story more believable, they may provide a fake customer list and telephone numbers (prepared in advance) to the investors for their verification. When the investors went on site to observe the production and operation situation, the firms will hire temporary workers, and put out samples for production, rent inventory and container trucks to temporarily boost production and shipments. When the investors find out that even if the production line of a factory were fully running, it would still not be able to produce the firm’s claimed revenue, the firm will attempt to keep the lie going by claiming that there are too many orders for their facilities to handle, so they have engaged some OEM (“Original Equipment Manufacturer”) factories in other cities. Finally, this small investment firm will talk to the long-term cooperating accounting/auditing firms to make sure that the fake financials pass through the auditing process smoothly, and that perfect audit reports will be issued for those companies. They will make sure those auditor reports seem very reliable. According to the falsified financial statements, invoices, bank statements and relevant government official seals in procession of the lawyers handling the case, this case reveals a systematically criminal platform which has been able to cheat even experienced US investors and the US SEC.

Typically, when the trainee companies at the “fraud school” successfully change from OTCBB to the main board stock exchange markets (NASDAQ/NYSE), the consulting/counselor companies, accounting/auditing firms, and the law firms serve in the previous stage will be replaced by larger and more reputable investment banks, auditing firms and lawyer firms, to attract larger investors and investments. When the investors finally figure out that they were being cheated, they usually blame the reputable accounting and law firms and the Chinese enterprises represented by them. Little do they know that the original initiator of the fraud—the “fraud school”— has withdrawn from its role and pocketed its money. This is behind the curtain while the US investors will never know.

Taking a real example, Dalian RINO, which is listed on NASDAQ, is an early graduate from the “fraud school”. RINO was found to have committed severe financial fraud in Nov. 2010, and was eventually delisted. The investors suffered a total loss of USD 800 million. The US SEC investigated the investment banks, accounting firms, and law firms that worked for RINO in the US and pursued severe liabilities against those large organizations. But most people are unaware that the seeds of financial fraud had already been planted several years ago by the “fraud school”. The US local investment bank, accountant firms and law firms are only scapegoats. According to a source, people in the same “fraud school” circle worked with FUSHI when it went public in the US. Even if there is no direct proof to show FUSHI is a fraud, people suspect that it is. According to an insider, FUSHI is going to delist itself. Some marketing analysts think this action may be due to the fact that FUSHI wants to avoid being supervised by the US market, stockholders and the SEC. The basis of the above theory is that FUSHI was sued and accused of fabricating financial data and misleading investors in a class action lawsuit. Forbes reported numerous fraud accusation proceedings, including an accusation against FUSHI during 2011, and assimilated these types of cases as the “Chinese version of Enron and WorldCom”.

After the RINO event, the US Congress paid attention to the fraud issues regarding the Chinese enterprises going public in the US, and conducted a detailed investigation into the investment banks, financial counsels, auditing firms and law firms which represent those Chinese enterprises. But nobody went far enough to shed light on the “fraud schools,” which initiated these fraudulent cases. Ms. Angela Zhang from Fair City, one of the companies that suffered from fraud, said: “In the past, it has just been foreigners who were cheated and lost money; but in this case, it is not just foreigners who lost money. The current investigation proves that Chinese authorities paid highly attention to such kind of cases, just like the US government inquiring into them in the US. As the leading lawyer of this case, Lawyer Yang represents the cheated investors in suing those suspected fraud enterprises, investment banks and auditing firms for damages. Lawyer Yang said “The on-going serious investigation into the “fraud school” will play an active role to restore the credit of the Chinese enterprises among investors, especially foreign investors”.

According to the official statistics of the US, the financial fraud committed by Chinese enterprises listed in US caused 35 billion USD in the past five years, and damaged the image and credit of China in the overseas financing market. Just as a stinky fish makes a pot of soup stinky, these fraudulent enterprises caused adverse effects among the “China Concept” stocks in the US market and forced many legitimate public company to suffer undue losses. This “winter of China concept stocks” may take several years to end in the US.