

Ignoring Severe Supply Chain Pollution

# **Xiaomi** Suspected of Violating IPO Disclosure Requirements



**IPE**

**PECC**

May 2018

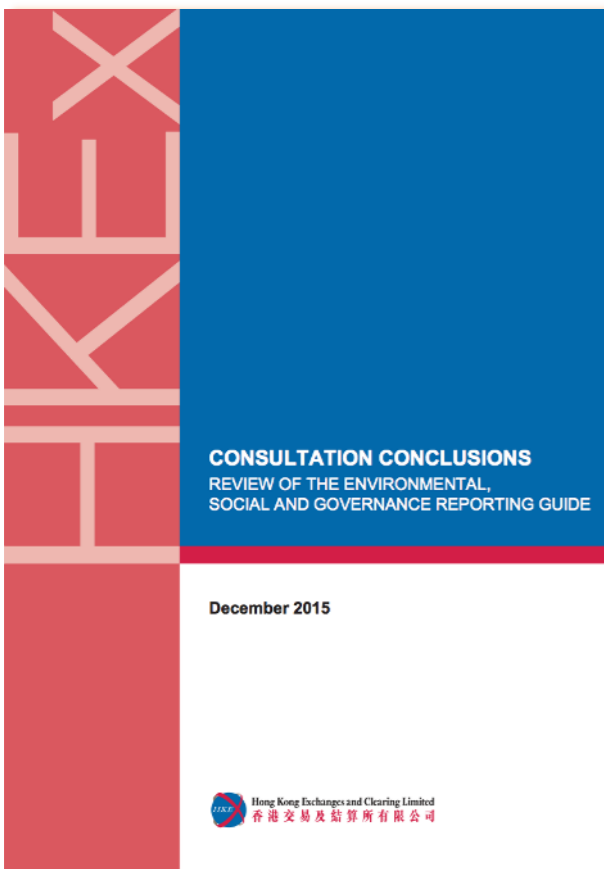
Xiaomi's recent submission of a prospectus to the Hong Kong Stock Exchange has taken major media headlines by storm. With \$10 billion in fundraising, Xiaomi is set to become one of the largest IPOs in Hong Kong's history.<sup>1</sup>

As a mainstream smartphone brand, Xiaomi has become a focus of both Chinese and foreign investors due to the success story of its product sales. This success is also the reason why Xiaomi's IPO has been so highly sought after by capital markets. But perhaps less known is that during Xiaomi's rapid expansion over the past four years, its supply chain has repeatedly encountered pollution-related problems. What's more, when facing concerns from environmental groups, Xiaomi has only been evasive and turned a blind eye.

A number of Chinese environmental groups recently completed another round of investigations into pollution in Xiaomi's supply chain. Compared with previous research, findings show that pollution has become even more severe. Groups once again raised these issues to Xiaomi, but still only received silence and avoidance in response.

Under the backdrop of global sustainable development, with Xiaomi to become a publicly-held listed company, its environmental, social and governance (ESG) performance is increasingly becoming a concern of investors and other stakeholders. And the Hong Kong Stock Exchange – where Xiaomi is seeking its IPO – has made clear requirements for ESG-related disclosure.

After reading Xiaomi's publicly-disclosed documents, we believe that Xiaomi is in violation of the Hong Kong Stock Exchange's relevant requirements for information disclosure.



## Hong Kong Stock Exchange's ESG Disclosure Requirements

The Stock Exchange of Hong Kong, Ltd. ("HKEX") issued its Consultation Paper: Review of the Environmental Social and Governance Reporting Guide (the "Guide") in July 2015.

In December 2015, the HKEX published the Consultation Conclusions: Review of the Environmental, Social and Governance Report Guide (see Figure 1), which confirms the main revisions to the Guide and requires issuers to refer to the revised Guide when disclosing ESG information for fiscal years beginning on or after January 1, 2016.

The main changes adopted are stipulated in the Consultation Conclusions as follows<sup>2</sup>:

**Figure 1. Consultation Conclusions: Review of the Environmental, Social and Governance Reporting Guide**

### Main changes adopted

In summary, the main changes include:

- (a) amending Rule 13.91 to require that:
  - (i) the issuer must state in its annual report or a separate ESG report whether it has complied with the "comply or explain" provisions set out in the ESG Guide for the relevant financial year;
  - (ii) where the issuer deviates from the "comply or explain" provisions, it must give considered reasons for doing so in its ESG report; and
  - (iii) the issuer must disclose its ESG information on an annual basis and regarding the same period covered in its annual report;
- (b) revising the introductory section of the Guide to provide more guidance on reporting and to be more in line with international standards;
- (c) re-arranging the Guide into two Subject Areas: A. Environmental and B. Social;
- (d) upgrading the General Disclosures under each Aspect of the Guide to "comply or explain";
- (e) revising the wording of the General Disclosures (where relevant) to be consistent with the directors' report requirements under the Companies Ordinance (Cap. 622 of the Laws of Hong Kong) ("CO") (which will be incorporated in the Listing Rules under Appendix 16, paragraph 28(2)(d), for financial years ending on or after 31 December 2015);
- (f) upgrading the Key Performance Indicators ("KPIs") under the "Environmental" Subject Area to "comply or explain"; and
- (g) revising the wording of the recommended (i.e. voluntary) disclosures of the Guide to bring it more in line with international standards of ESG reporting by incorporating disclosure of gender diversity.

### Implementation dates

The Rule amendments and the upgrade of the General Disclosures under each Aspect of the Guide from recommended to "comply or explain", as well as the revised recommended disclosures, will be effective for issuers' financial years commencing on or after 1 January 2016, as originally proposed (see paragraph 9 of the Consultation Paper).

In relation to the Environmental KPIs, we note concerns that the proposed implementation date would give issuers with December financial year-ends very short notice. In view of these concerns and considering that over 70% of our issuers have December financial year-ends, we have decided to postpone the implementation date for the upgrade of the Environmental KPIs to "comply or explain" by one year. The implementation of the upgrade will instead be for issuers' financial years commencing on or after 1 January 2017.

<sup>1</sup> [http://finance.ifeng.com/a/20180430/16223514\\_0.shtml](http://finance.ifeng.com/a/20180430/16223514_0.shtml) (All links in this article were accessed on May 19, 2018)

<sup>2</sup> [https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2011-to-2015/July-2015-Consultation-](https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2011-to-2015/July-2015-Consultation-Paper/Conclusions/cp201507cc.PDF)

[Pape/Conclusions/cp201507cc.PDF](https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2011-to-2015/July-2015-Consultation-Paper/Conclusions/cp201507cc.PDF)

According to the revised Environmental Social and Governance Reporting Guide, “policies on managing environmental and social risks of the supply chain” fall under “General Disclosures,” and companies have a responsibility to “comply or explain.”

While searching Xiaomi’s website and other public documents that we could locate, we were unable to find Xiaomi’s disclosure of its “policies on managing environmental and social risks of the supply chain.”

So, does Xiaomi’s supply chain have environmental risks that require disclosure?

New Guide			
	“Comply or explain” Provisions	Recommended Disclosures	
<b>Aspect B4: Labour Standards</b>	General Disclosure Information on: (a) the policies; and (b) compliance with relevant laws and regulations that have a significant impact on the issuer relating to preventing child and forced labour.		
		KPI B4.1	Description of measures to review employment practices to avoid child and forced labour.
		KPI B4.2	Description of steps taken to eliminate such practices when discovered.
<b>Operating Practices</b>			
<b>Aspect B5: Supply Chain Management</b>	General Disclosure Policies on managing environmental and social risks of the supply chain.		
		KPI B5.1	Number of suppliers by geographical region.
		KPI B5.2	Description of practices relating to engaging suppliers, number of suppliers where the practices are being implemented, how they are implemented and monitored.

Figure 2. Disclosure requirements for “supply chain management” in the Review of the Environmental, Social and Governance Reporting Guide

## Suspected Supplier of Flexible Circuit Boards to Xiaomi Found to Repeatedly Discharge Wastewater Illegally

Ichia Technology (Suzhou) Co., Ltd (“Ichia Suzhou”) is a wholly-owned subsidiary of Taiwanese company Ichia Technologies, Inc. (“Ichia Technologies”) that is located in mainland China<sup>3</sup> (see Figure 3).



Figure 3. Ichia Technologies global deployment

Referencing the National Enterprise Credit Information Publicity System<sup>4</sup>, the business scope of Ichia Suzhou includes the following: development and production of flexible circuit boards, control panels and other components used in instruments and telecommunications devices and materials, precision molds, photoelectric conversion devices and other key parts of digital cameras and related products; development and production of precision aluminum-magnesium alloy molding products and other various types of new materials.

According to public materials, Ichia Technologies established a supplier-customer relationship with Xiaomi in 2013.<sup>5</sup>

<sup>3</sup> [http://www.ichia.com/index.php?option=com\\_content&view=article&id=593&Itemid=1280&lang=en](http://www.ichia.com/index.php?option=com_content&view=article&id=593&Itemid=1280&lang=en)  
<sup>4</sup> <http://www.gsxt.gov.cn/index.html>

<sup>5</sup> <http://www.chinatimes.com/cn/newspapers/20131128000170-260206>

According to an article published by the China Times on June 3, 2014<sup>6</sup>, "Ichia (2402) announced that its May revenue reached 1.042 billion TWD, which hit a new record compared with the same period in previous years. Ichia grew at an annual rate of 19 percent, and its revenue from flexible printed circuit (FPC) components reached 932 million TWD – the second highest level this year and the third highest on record in history. Industry experts pointed out that Ichia is a supplier to Xiaomi. This year, Xiaomi has already built and shipped 60 million mobile phones, and Ichia is expected to be a beneficiary" (Figure 4).

In April 2018, the Business Times published another piece indicating that Ichia Technologies is a supplier of flexible printed circuit boards used in Xiaomi cell phones<sup>7</sup> (Figure 5).

The screenshot shows a news article from the China Times dated June 3, 2014. The main headline is "毅嘉5月營收 創同期新高 年增率近2成". The article text states that Ichia (2402) announced its May revenue of 1.042 billion TWD, a new record, with a 19% year-over-year increase. It highlights that revenue from flexible printed circuit (FPC) components reached 932 million TWD, the second highest level this year and the third highest on record. The article also mentions that Ichia is a supplier to Xiaomi, which has shipped 60 million mobile phones this year. Social media sharing icons for Facebook, Google+, Twitter, and Weibo are visible. A sidebar on the left contains other news items like "國巨挺進千金 被動元件類股成新貴" and "搶救低薪 賴揆擬調高時薪至150元".

Figure 4. China Times report in 2014

## 毅嘉3月營收月增65%

2018年04月03日 04:10 工商時報 吳筱雯 / 台北報導

工作天數回復正常、汽車用軟板出貨增加，毅嘉（2402）3月營收總算回到6.14億元，比飽受農曆年影響的2月營收大增65%，也比去年同期增加9%，第一季營收為15.93億元，較去年同期成長8%。不過法人仍強調，第1季產能利用率不高、新台幣兌美元匯率仍相對強勢，毅嘉首季能否擺脫虧損仍有待觀察。

毅嘉去年重返手機用軟板市場後，雖然營收水準明顯揚升，可是在中國手機品牌客戶常在最後一刻修改線路、導致毅嘉量產良率不高，手機軟板價格也偏低，加上高毛利的汽車用軟板本來穩定成長，然而受到客戶延續數個月的庫存調整，表現不如預期，都讓毅嘉去年一整年營收都好看，可本業都沒有獲利。

不過，今年以來汽車軟板拉貨力道恢復不少，農曆年假因素也已經結束，帶動3月營收回復至6.14億元，比去年同期成長9%，首季營收為15.93億元，也比去年同期增加8%。

法人表示，車用軟板出貨不佳，去年車用佔軟板營收比重一度降至35%上下，不過目前已經回到5成，今年車用軟板營收與佔比都有機會持續向上走，而手機用軟板雖然已打入OPPO、華為、小米等中國一線品牌，被中國品牌接手的黑莓機去年下半年也對毅嘉下單積極，然而今年以來拉貨最積極的手機客戶，其實是經營諾基亞手機品牌的HMD，今年手機用軟板可能比較辛苦。

Figure 5. China Times report in 2018

<sup>6</sup> <http://www.chinatimes.com/newspapers/20140603000151-260206>

<sup>7</sup> <http://www.chinatimes.com/print/newspapers/20180403000383-260206>

In May 2018, Lüse Jiangnan Public Environment Concerned Center (“PECC,” or also denoted as “Lüse Jiangnan”) and the Institute of Public & Environmental Affairs (IPE) conducted a joint investigation into Ichia Suzhou.

On the afternoon of May 12, from the vantage point of the Dian Bridge on the north side of Ichia Suzhou, staff from Lüse Jiangnan and IPE observed and found a situation whereby effluent was draining from the wall of the west area of Ichia Suzhou into the river channel (Figure 6). The drainage location was about 100 meters away from the Dian Bridge (Figure 7).

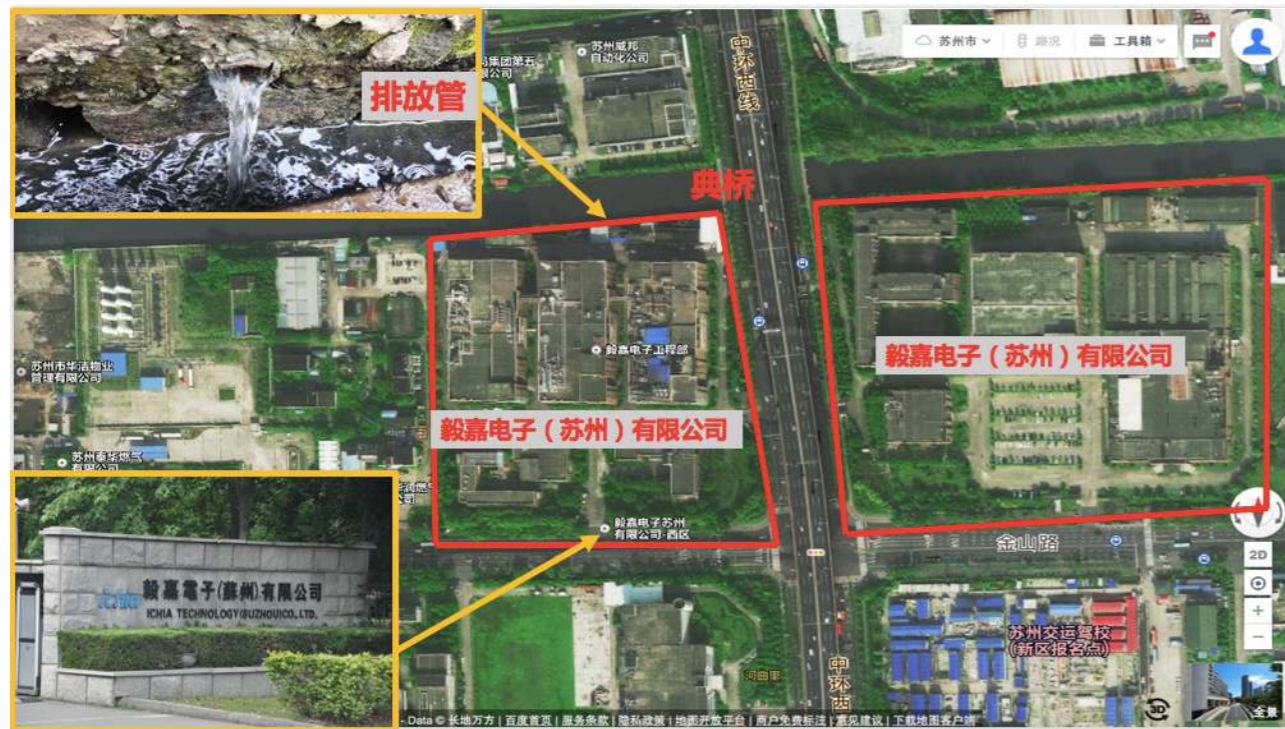


Figure 6. Location of Ichia Suzhou



Figure 7. Location of hidden pipe

In order to sample the drainage, Lüse Jiangnan staff borrowed a small boat to get nearer to the drainage location. Closer observations revealed that on the side of the stone wall facing the river, a pipe extending from the stone wall of Ichia Suzhou’s wastewater treatment station was discharging water into the river. Lüse Jiangnan’s staff took on-site samples from the pipe and photographed it.



Figure 8. Lüse Jiangnan staff found this pipe discharging water

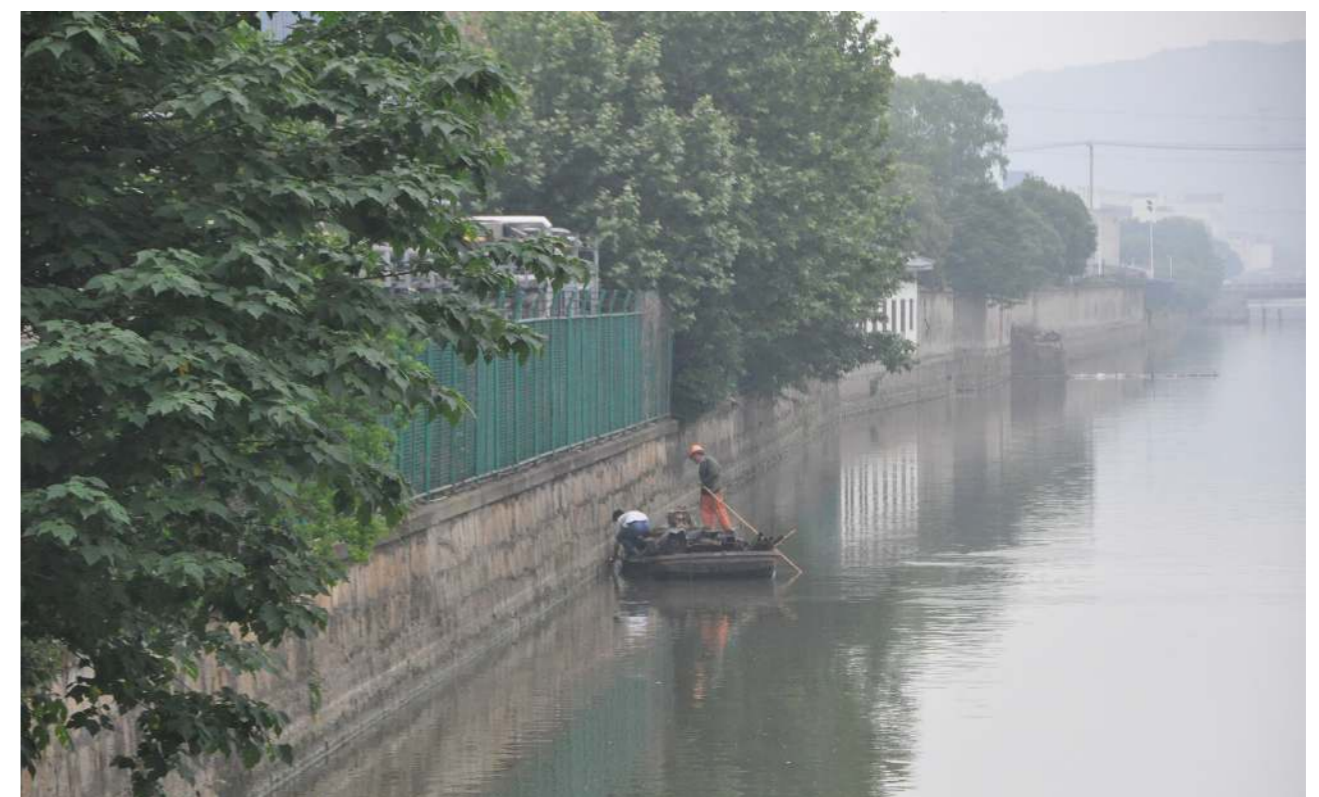


Figure 9-1. Lüse Jiangnan staff collecting samples on site



Figure 9-2. Lüse Jiangnan staff collecting samples on site

Lüse Jiangnan and IPE staff used pH test paper to test the water samples collected at the site. Comparisons showed the pH values to fall between 2 and 3, indicating relatively strong acidity (see Figure 10).

Lüse Jiangnan staff then sent the water samples to a qualified third-party testing agency, Bureau Veritas (Shanghai) Co., Ltd., for analysis (see Figure 11).



Figure 11-1. Sample sent to BV

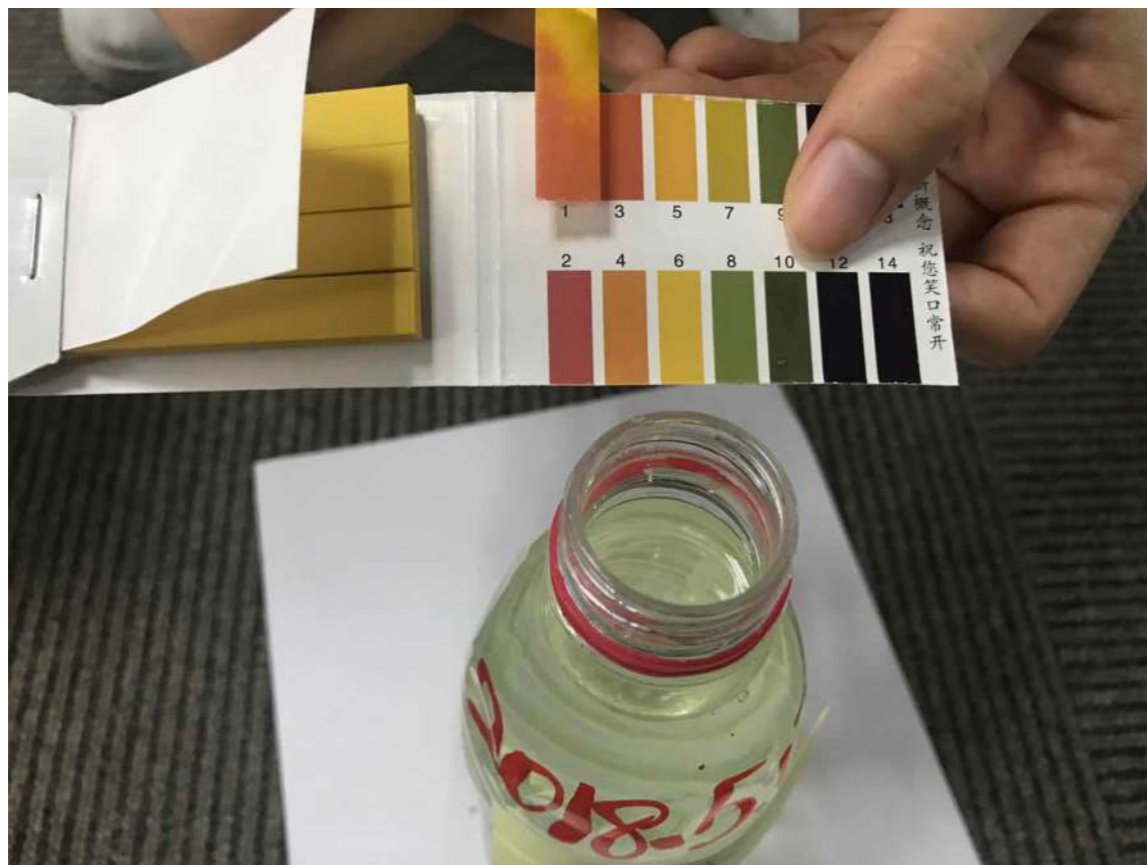


Figure 10. Test results of pH level



LAB NO. : (6618)134-0537  
 DATE : May 15, 2018  
 PAGE : 4 OF 4

测试结果

基质: 水

项目	单位	方法检出限	废水
			无色液体
			66181340537-01
pH	---	0.01	2.64
砷	µg/L	0.12	2.06
镉	µg/L	0.05	0.93
铬	µg/L	0.11	84.3
铜	µg/L	0.08	5.86×10 <sup>4</sup>
铅	µg/L	0.09	24.9
镍	µg/L	0.06	53.8
锌	µg/L	0.67	283
汞	µg/L	0.05	<0.05
锰	µg/L	0.12	452
铁	µg/L	0.82	8.42×10 <sup>3</sup>
镁	µg/L	1.94	8.51×10 <sup>3</sup>
铝	µg/L	1.15	1.82×10 <sup>3</sup>
化学需氧量	mg/L	4	349
六价铬	mg/L	0.004	<0.004

备注: <: 小于最低检出浓度。

END

Figure 11-2. Test results of water sample sent to BV

According to the 2014 Commissioned Testing Report (2014) Suzhou State Environmental Monitoring (Commissioned) No. 634<sup>8</sup> disclosed by Ichia Suzhou, levels of Copper (Cu) and Nickel (Ni) in Ichia Suzhou's wastewater discharge should refer to the standard limit values laid out in Table 3 in the Emission Standard of Pollutants for Electroplating – GB 21900-2008, with the rest of indicators all referring to the standard limit values requirements laid out in Table 4, Class 3 of the Integrated Wastewater Discharge Standard – GB 8978-1996.

<sup>8</sup> [http://www.woa.ipe.org.cn/Upload/file/企业反馈/毅嘉电子\(苏州\)有限公司/2014年度委託環境監測.pdf](http://www.woa.ipe.org.cn/Upload/file/企业反馈/毅嘉电子(苏州)有限公司/2014年度委託環境監測.pdf)

<sup>9</sup> Wastewater was discharged directly into waters in the natural environment through the hidden drainage pipe. As Suzhou is under the jurisdiction of Taihu area, according to the Table 3 Main Water Pollutants Discharge Limits for Key Industries of Taihu Area in the Discharge Standard of Main Water Pollutants for Municipal Wastewater Treatment Plant and Key Industries of Taihu Area (DB32/1072-2007), the discharge limit for COD for the electroplating industry

Comparing the inspection results of Bureau Veritas with the aforementioned standards (Table 1), the copper concentration in the sample exceeded the standard by 195 times, and the pH value was 2.64, which is out of compliance with the standard value range of 6 - 9. Ichia Suzhou is thus suspected of discharging acidic, copper-containing wastewater through a hidden pipe.<sup>9</sup>

Table 1. Ichia Suzhou test results in comparison to discharge standards

Wastewater Pollutants	Unit	BV Test Results	Emissions Standard of Pollutants for Electroplating GB21900-2008 Table 3 Special Discharge Limits for Water Pollutants	Integrated Wastewater Discharge Standard GB 8978-1996 Table 4, Class 3
pH	-	2.64	6-9	
Cu	µg/L	58600	300 (Enterprise discharge outlet)	
Ni	µg/L	53.8	100 (Wastewater discharge outlet in production workshop or facilities)	
COD	mg/L	349		500

Searches of the Blue Map Database show that Ichia Suzhou has received a number of negative environmental records since 2014 (Table 2).<sup>10</sup> In March 2018, Ichia Suzhou was also fined 117,000 RMB (Figure 12)<sup>11</sup> by the Suzhou Environmental Protection Bureau for discharging wastewater with pollutants in excess of standards.

苏州市环境保护局  
 苏州市太湖流域水污染防治办公室

当前位置: 首页 > 苏州市环保局行政许可和行政处罚等信用信息公示专栏 > 行政处罚公示

苏州市环保局行政许可  
 行政处罚公示  
 双公示目录

苏环行罚字(2018)第15号毅嘉电子(苏州)有限公司超标排放水污染物案

【信息时间: 2018/3/8 阅读次数: 243】【我要打印】【关闭】

处罚名称:	毅嘉电子(苏州)有限公司超标排放水污染物案
行政处罚决定书文号:	苏环行罚字(2018)第15号
处罚事由:	超标排放水污染物
处罚依据:	《中华人民共和国水污染防治法》(2008年)第七十四条第一款

Figure 12. 2018 case of Ichia Suzhou's excessive discharge of water pollutants

is 80mg/L; therefore, Ichia is suspected of excessive discharge of COD.

<sup>10</sup> [www.woa.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=38058&dataType=0&isyh=0](http://www.woa.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=38058&dataType=0&isyh=0)

<sup>11</sup> <http://www.szhbj.gov.cn/hbj/infodetail/?infoId=f3e10f21-f09e-49be-82a4-6175b1fd54f1&categoryNum=040002>

Table 2. Ichia Suzhou environmental violation records since 2014

Time of Penalty	Environmental Violation(s)
2018	Wastewater pollutant discharge exceeded legal standards
2017	Failed to enact emergency contingency measures after the occurrence of water pollution incident
2016	Excessive discharge; Failed to enact emergency contingency measures after the occurrence of water pollution incident; Temporary rental workshop of Ichia Suzhou began operation prior to inspection
2014	Excessive discharge of water pollutants; Rated as a “yellow” enterprise by the environmental credit system for non-state monitored enterprises

## More Suspected Suppliers to Xiaomi See Environmental Violations

Apart from Ichia Suzhou, checks on the environmental compliance of Xiaomi supply chain revealed that many suspected suppliers of core components for Xiaomi’s mobile phones have exhibited varying degrees of illegal environmental behavior in recent years.

### 1. Century Technology (Shenzhen) Co., Ltd.: Suspected supplier of display panels to Xiaomi<sup>12 13 14</sup>

Enterprise Name	Environmental Violation(s)
Century Technology (Shenzhen) Co., Ltd.	2017: - Wastewater outlet pH level exceeded legal standards; - Discharge outlet was set in violation of regulations, failed to properly install online monitoring equipment; 2015: Exhaust gas emissions disturbing local residents

### 2. Tongda Group: Suspected supplier of phone casings to Xiaomi<sup>15 16 17</sup>

Enterprise Name	Environmental Violation(s)
Tongda (Xiamen) Smart Tech Industry Co., Ltd.	2016: “Exhaust gas monitoring result (average value) shows...concentration of non-methane hydrocarbon reached 126 mg/m3...Based on your company’s environment functional area (type II) and construction project conditions, standards listed in Table 1 of the Xiamen Air Pollutant Emission Standards (DB35/323-2011) apply: the concentration of non-methane hydrocarbon should not exceed 100 mg/m3 ... therefore, your company’s air emissions exceeded legal standards; the pollutant exceeding the standard is non-methane hydrocarbon.”

<sup>12</sup> <http://news.hiapk.com/xiaomi/1639735.html>

<sup>13</sup> [https://weibo.com/1651911632/G8T9eyiUZ?filter=hot&root\\_comment\\_id=0&type=comment](https://weibo.com/1651911632/G8T9eyiUZ?filter=hot&root_comment_id=0&type=comment)

<sup>14</sup> <http://www.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=183107&dataType=0&isyh=0>

<sup>15</sup> <http://www.tongda.com/index.php/en/about-tongda-group/company-overview>

<sup>16</sup> <http://www.hkexnews.hk/listedco/listconews/SEHK/2018/0413/LTN20180413173.pdf>

<sup>17</sup> <http://www.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=304373&dataType=0&isyh=0>

<sup>18</sup> <http://gubaf10.eastmoney.com/news,300115,741220977.html>

### 3. Everwin Precision: Suspected supplier of ceramic exterior parts for mobile phones to Xiaomi (Figure 13)<sup>18 19 20</sup>

Enterprise Name	Environmental Violation(s)
Kunshan Everwin Precision Technology Co., Ltd.	2016: - Excessive discharge of water pollutants - Project of “consumer electronics with an annual increase in production of 30 million exterior parts” began operation prior to inspection - Rated as a “yellow” enterprise by the environmental credit system
Shenzhen Everwin Precision Technology Co., Ltd. (Die casting factory)	2015: COD level at the discharge outlet exceeded legal standards by 1.19 times; phosphate concentration exceeded legal standards by 6.18 times

The screenshot shows a forum post on the East Money website. The user '长盈精密吧' (Changying Precision Bar) posted on 2018-01-08 at 17:41:00. The post asks: '董秘您好，据媒体报道小米将在香港上市，能否介绍下目前我们公司和小米的合作关系。' (Dear Secretary, according to media reports Xiaomi will be listed in Hong Kong, can you introduce the current cooperation relationship between our company and Xiaomi?). A reply from '长盈精密' (Changying Precision) on 2018-01-12 at 18:36:00 states: '您好。公司与小米长期保持着较好合作关系，已向小米提供多款其米系列手机的外观件产品。谢谢。' (Hello. Our company has maintained a good long-term cooperation relationship with Xiaomi, and has provided Xiaomi with multiple external components products for its Mi series mobile phones. Thank you.)

Figure 13. Everwin Precision BBS on the East Money website

### 4. Wingtech Group: Suspected ODM supplier to Xiaomi<sup>21 22 23</sup>

Enterprise Name	Environmental Violation
Wingtech Group	2016: Began operation prior to inspection
Wingtech Group (Communications Industry Base)	2016: Began operation prior to inspection

<sup>19</sup> <http://www.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=143167&dataType=0&isyh=0>

<sup>20</sup> <http://www.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=296892&dataType=0&isyh=0>

<sup>21</sup> <http://www.wingtech.com/en>

<sup>22</sup> <http://www.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=187631&dataType=0&isyh=0>

<sup>23</sup> <http://www.ipe.org.cn/IndustryRecord/regulatory-record.aspx?companyId=1276449&dataType=0&isyh=0>



## Has Xiaomi Met HKEX Requirements to “Comply or Explain”?

Based on the above research, it is clear that Xiaomi’s supply chain may pose environmental risks, and some suspected suppliers have repeatedly exceeded the discharge standards for certain pollutants, resulting in relatively high environmental risks.

As a result, Xiaomi has not fulfilled the relevant requirements of the Hong Kong Stock Exchange for companies to disclose their “policies on managing environmental and social risks of the supply chain.”

But has Xiaomi met the requirement of the Guide to “comply or explain”?

In Xiaomi’s prospectus, we see the following such statement<sup>24</sup>:

### Health, Safety and Environmental Matters

We engage outsourcing partners to assemble our hardware products developed in-house and rely on partners to supply finished ecosystem hardware products. We do not operate any manufacturing or assembling facilities. We only operate some of the key warehouses and engage third parties for delivery of our products. Therefore, we are not subject to significant health, safety or environmental risks. To ensure compliance with applicable laws and regulations, from time to time, our human resources department would, if necessary and after consultation with our legal advisors, adjust our human resources policies to accommodate material changes to relevant labor and safety laws and regulations. During the Track Record Period and up to the Latest Practicable Date, we had not been subject to any material fines or other penalties due to non-compliance with health, safety or environmental regulations.

Xiaomi emphasizes, “We do not operate any manufacturing or assembling facilities. We only operate some of the key warehouses and engage third parties for delivery of our products.” So is Xiaomi bound to abide by the disclosure obligation for “policies on managing environmental and social risks of the supply chain”?

Actually, the first part of this statement clearly asserts that Xiaomi’s revenue-creating mobile phones and eco-chain hardware products are all assembled by employing partners and relying on partners to supply them. These companies naturally must be regarded as part of Xiaomi’s supply chain, and Xiaomi must also assume responsibility for “policies on managing environmental and social risks of the supply chain”.

According to the HKEX Listing Rules<sup>25</sup>, Article 13.91 stipulates the following<sup>26</sup>:

- 13.91 (1) The Environmental, Social and Governance (“ESG”) Reporting Guide in Appendix 27 comprises two levels of disclosure obligations: (a) “comply or explain” provisions; and (b) recommended disclosures.
- (2) Issuers must state whether they have complied with the “comply or explain” provisions set out in the ESG Reporting Guide for the relevant financial year in their annual reports or in separate ESG reports.
- (3) Where the issuer deviates from the “comply or explain” provisions, it must give considered reasons in its ESG report.

Xiaomi has already evaded the “comply or explain” provisions.” Then has Xiaomi complied with the requirement to “give considered reasons in its ESG report”?

Based on checks of Xiaomi’s website and other publicly-available documents, we could not find Xiaomi’s “considered reasons.”

<sup>24</sup> <http://www.hkexnews.hk/APP/SEHK/2018/2018050202/Documents/SEHK201805030005.pdf>

<sup>25</sup> [http://en-rules.hkex.com.hk/net\\_file\\_store/new\\_rulebooks/c/o/consol\\_mb.pdf](http://en-rules.hkex.com.hk/net_file_store/new_rulebooks/c/o/consol_mb.pdf)

<sup>26</sup> The Listing Rules define “issuer” as any company or other legal person any of whose equity or debt securities are the subject of an application for listing.

<sup>27</sup> [https://weibo.com/5136788508/C11JiYUO?from=page\\_1006065136788508\\_profile&wvr=6&mod=weibotime](https://weibo.com/5136788508/C11JiYUO?from=page_1006065136788508_profile&wvr=6&mod=weibotime). English translation: “Thank you @Blue

## Are These Alleged Breaches of Disclosure Accidental or Deliberate?

Since 2014, environmental organizations have sent letters to Xiaomi every year, hoping to communicate about the pollution issues in its supply chain – but there was only once a more formal response from Xiaomi. Analysis of this response shows that the lack of relevant information in Xiaomi’s prospectus is not an accidental error, but is rather due to Xiaomi’s deep consideration.

In 2015, seven environmental groups sent letters to Lei Jun, the president of Xiaomi, regarding environmental pollution in Xiaomi’s supply chain.

Year	Number of suspected suppliers with violations involved	Xiaomi response
May 2014	2	N/A
March 2015	10	N/A
June 2015	11	Yes
April 2016	IPE contacted Xiaomi regarding its CITI score, but no specific suppliers mentioned	N/A
July 2017		N/A

On June 4, 2015, IPE published a WeChat article entitled, “[Environment Day] Xiaomi, Are You OK?”. The article points out that the manufacturing process of IT products also gives off a lot of pollution, including toxic and hazardous substances, and may be harmful to the environment and public health.

The WeChat article emphasizes: “Xiaomi’s sales are astonishing, but its environmental protection is shocking.” In the first quarter of 2015, Xiaomi’s smart phone sales ranked second, but from the perspective of environmental performance, Xiaomi was the only brand out of the 37 IT brands evaluated by the Corporate Information Transparency Index (CITI) green supply chain evaluation that completely refused to face up to issues of pollution in its supply chain, scoring zero points and ranking at the very bottom.

In the article, IPE introduces that “since May 2014, environmental protection organizations have repeatedly sent letters to Xiaomi, hoping to communicate about issues concerning pollution in its supply chain, but none of these letters came to anything.” Ichia Suzhou is among the suspected Xiaomi suppliers listed in the article (Figure 14).

The WeChat article reminded Xiaomi not to “make pollution expand along with increasing sales,” since “if the pollution from its own manufacturing processes cannot be effectively controlled, then the higher the output of Xiaomi, the greater the pollution discharge may become.” “If Xiaomi continues to ignore pollution, we are afraid that even more people will become victims of industrial pollution.”

On the day that IPE’s WeChat article was published, Xiaomi issued the following response via its “Xiaomi Spokesperson” Weibo<sup>27</sup>:



Map and other environmental groups for your attention. Environmental protection is of great importance to Xiaomi, and we ourselves have been promoting environmental protection. As an internet company focusing on research and development of smartphones, we do not engage in manufacturing. We select the same top global supply chain companies chosen by Apple and Samsung, etc., for strategic cooperation. We will convey the suggestions from environmental groups to our supply chain companies and urge them to take measures to improve. #Protect the blue sky with Xiaomi Fans.”

It can be seen from this response that Xiaomi expresses itself in the first place as “an internet company focusing on research and development of smartphones that does not engage in manufacturing.”

More importantly, Xiaomi emphasizes that, “we select the same top global supply chain companies chosen by Apple and Samsung, etc., for strategic cooperation.” The subtext of this statement seems to indicate that Xiaomi chooses supply chain companies used by leading brands, and can thus free ride on their supply chain environmental risk management.

However, unlike Apple, Samsung and other international brands as well as Huawei and other domestic industry peers, Xiaomi only copies the OEM model of these brands, but does not actually emulate these leading brands by assuming responsibility for supply chain environmental management.

In recent years, the significant expansion of government and corporate environmental information disclosure means that corporate environmental supervision records can be publicly accessed. Leading brands such as Apple, Dell, and Huawei have begun to use this information to evaluate suppliers’ environmental performance and discern supply chain environmental compliance risks. Through green procurement, they have motivated suppliers to adopt corrective measures to reduce the burden that their production poses on the environment.

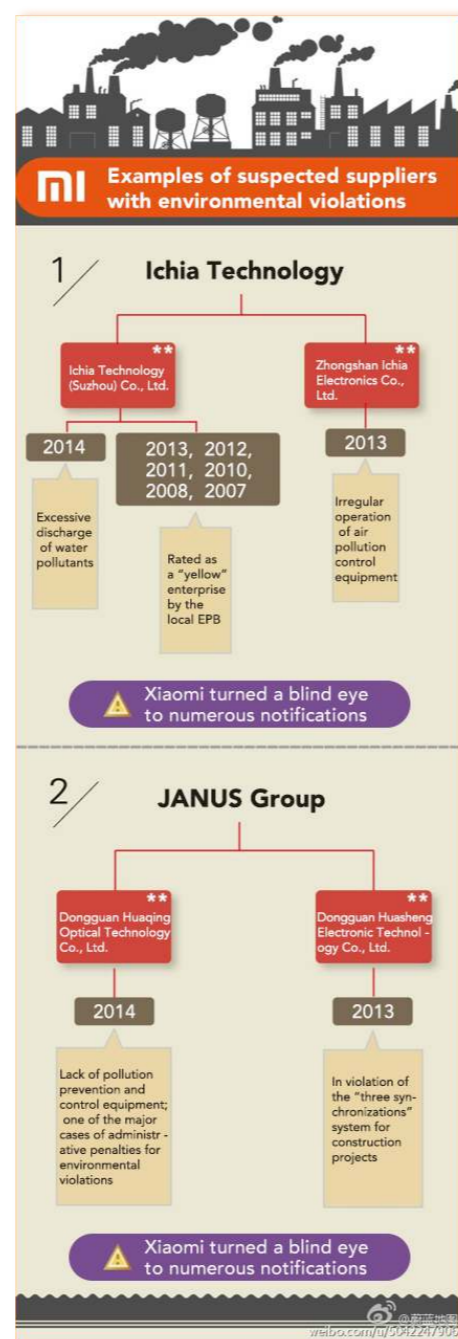
Some leading brands have even begun to extend environmental compliance and risk management to upstream suppliers, touching on production of metals and other raw materials, centralized wastewater treatment, and hazardous waste treatment. They have also motivated suppliers to disclose annual data on pollutant emissions and transfer.

While several leading global IT brands have cooperated with Chinese environmental organizations and prompted thousands of suppliers to implement rectifications or disclose relevant data, Xiaomi has not made any additional public follow-up explanation as to whether it will heed environmental groups’ recommendation to “provide feedback to cooperating enterprises in its supply chain, and urge them to adopt measures to improve.” What’s more, Xiaomi has not responded to environmental groups’ recommendations to establish a supply chain environmental management system.

On May 15, 2018, six environmental organizations – Lüse Jiangnan, EnviroFriends, Green Hunan, Friends of Nature, Green Qilu and IPE – again sent a joint letter to Xiaomi.

On May 16, the express delivery courier had been signed as received. However, up through the time of publication, we have yet to receive a response from Xiaomi.

Figure 14. Suspected suppliers to Xiaomi listed in [Environment Day] Xiaomi, Are You OK?



<sup>28</sup> [http://auto.sina.com.cn/j\\_kandian.d.html?docid=fykyfwq8423967&subch=iauto](http://auto.sina.com.cn/j_kandian.d.html?docid=fykyfwq8423967&subch=iauto)

## Do Supply Chain Environmental Risks Bring About Investment Risks?

In confronting smog and water pollution, Xiaomi is keen to smell business opportunities. Early on, it had already launched a variety of air and water purifying products. However, searches of Xiaomi’s official website have been unable to locate any commitment to environmental responsibility. This makes Xiaomi an outlier among leading global brands.

Without any environmental commitments, there is little impetus to invest in resources to control pollution, and costs can theoretically be reduced, which is very much in line with Xiaomi’s business model of controlling operating costs. However, with China’s current efforts to strengthen environmental enforcement, for an IT brand lacking an environmental management system, supply chain environmental risks may become financial risks, which then turn into investment risks.

Faced with severe air, water and soil pollution, China has already launched a massive environmental enforcement drive. Strengthening environmental supervision has become an irreversible trend.

During the “Schaeffler supply chain incident” affecting the automotive industry in September 2017, the CEO of Schaeffler declared that the suspension of production at a supplier of needle roller bearings may cause the industry 300 billion RMB in losses<sup>28</sup> (Figure 15).

Although losses of 300 billion RMB proved to be an exaggeration, the incident still made more people realize that a brand which disregards supply chain pollution and lacks an environmental management system for its supply chain, yet has environmental risks in its supply chain, may also be exposed to business and financial risks.

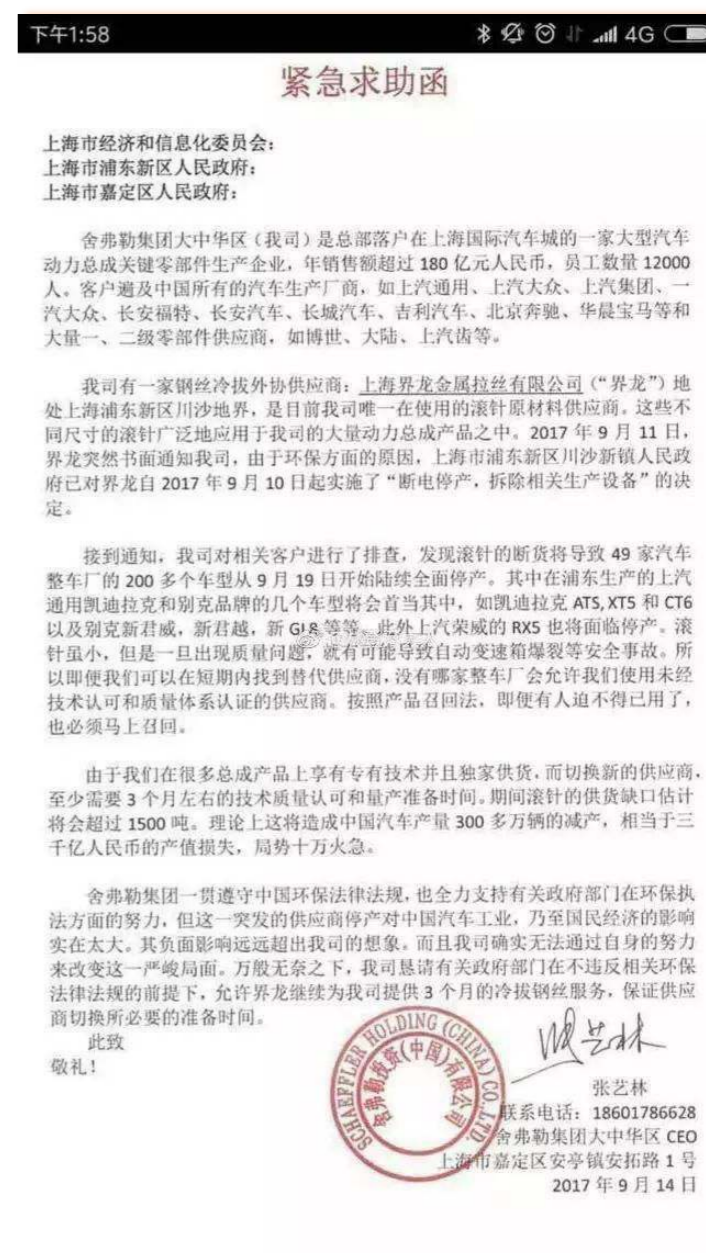


Figure 15. An open letter from Schaeffler

## Recommendations for Resolving Supply Chain Pollution and Information Disclosure Infractions

On July 1, 2017, the China Securities Regulatory Commission (CSRC) stated that those who have received administrative penalties relating to environmental protection within the past 36 months, in serious cases, may not publicly issue shares. Some companies' IPOs have been denied due to repeated environmental violations.

Xiaomi has positioned itself as “an internet company with smartphones and smart hardware connected by an IoT platform at its core.”<sup>29</sup>

However, according to media reports, Xiaomi's prospectus shows that smartphones (hardware) accounted for 80.4%, 71.3% and 70.3% of its revenue, respectively, over the past three years (2015, 2016 and 2017). If Xiaomi's so-called IoT (internet of things) and consumer products businesses (which are also primarily hardware) are also considered – which respectively accounted for 13.0 %, 18.1% and 20.5% of total revenue over the past three years – then Xiaomi's revenue from hardware is as high as 90.8%.<sup>30</sup>

All along, Xiaomi has grabbed market share for mobile phones by using cost controls and low prices as selling points. However, to what extent have these low costs been achieved at the expense of the environment and health?

Does such a company that repeatedly avoids pollution problems and clearly lacks environmental controls in its supply chain pose a potential investment risk with today's continual strengthening of environmental supervision and constantly rising risks of illegal behavior in the supply chain?

Does a company that fails to meet IPO information disclosure requirements conform to the criteria for initial public offerings?

In response to these questions, we make the following recommendations:

### 1. Xiaomi:

- Fulfill IPO disclosure requirements for “policies on managing environmental and social risks of the supply chain” put forth by the Hong Kong Stock Exchange;
- Issue public explanations about environmental violation issues at suspected suppliers raised by environmental groups;
- Begin to establish an effective supply chain environmental management system;

### 2. Xiaomi's Suppliers:

- Issue public explanations of corrective action plans and their results in response to environmental violation records;
- Strictly comply with environmental protection laws and regulations and perform environmental information disclosure obligations in accordance with the law;

### 3. Hong Kong Stock Exchange:

- Ensure that companies making IPOs fulfill the disclosure requirements for “policies on managing environmental and social risks of the supply chain” in their relevant documents;
- Effectively protect the public's right-to-know and safeguard the rights and interests of investors;

### 4. Investors:

- Pay attention to whether companies making IPOs have implemented relatively comprehensive environmental management systems;
- Focus on the impact of environmental violations on the supply chain stability of listed companies, and beware of environmental risks that may turn into investment risks;

### 5. The Public and Consumers:

- Pay attention to the environmental compliance and pollution control issues of companies themselves and their supply chains;
- Use one's purchasing power to make green choices and leverage green consumption to guide corporations toward green production.

*Translation Accuracy Disclaimer: This document has been translated by IPE for the purposes of reference only. Due to the difficulties of translation, slight differences may exist. If any questions arise related to the accuracy of the information contained in this translation, please refer to the Chinese version of the document, which is the official version of the document. Any discrepancies or differences created in the translation are not binding and have no legal effect for compliance or enforcement purposes.*

(About the source of the cover image: The cover image of this investigation report was originally a poster published by the Xiaomi Exploration Laboratory: [https://weibo.com/5833671738/FeuktXR2n?from=page\\_1006065833671738\\_profile&wvr=6&mod=weibotime](https://weibo.com/5833671738/FeuktXR2n?from=page_1006065833671738_profile&wvr=6&mod=weibotime) It mentioned that “Recalling the past is to learn from history; exploring tomorrow is to better meet the future.” We also hope to take this opportunity to discuss with Xiaomi about its responsibility for the environment and the future. We tried to contact the author of the image but failed. If the author sees this, please contact us at [ipe@ipe.org.cn](mailto:ipe@ipe.org.cn) or 010-67189470.)

<sup>29</sup> <https://www.mi.com/en/ir/>

<sup>30</sup> [http://m.sohu.com/a/231320576\\_120702](http://m.sohu.com/a/231320576_120702)