



THE STOCK EXCHANGE OF HONG KONG LIMITED

(A wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited)
(the “Exchange”)

27 August 2008

The Listing Committee of The Stock Exchange of Hong Kong Limited (the “Listing Committee”) censures the following parties for breaching the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Exchange Listing Rules”):

- 1. China Water Industry Group Limited (the “Company”) (Stock code: 1129);**
- 2. Mr Sze Chun Ning, an executive director of the Company (“Mr Sze”); and**
- 3. Mr Shi De Mao, an executive director of the Company (“Mr Shi”).**

On 17 June 2008, the Listing Committee conducted a hearing into the conduct of, among others, the Company, Mr Sze and Mr Shi in relation to their respective obligations under the Exchange Listing Rules and the Declaration and Undertaking with regard to Directors given by each of the relevant directors to the Exchange in the form set out in Appendix 5B to the Exchange Listing Rules (the “Director’s Undertaking”).

Facts

The Onfar Project

Prior to July 2006, the Company did not engage in any water supply or sewage treatment or related business. In 2006, the Company began looking for measures to diversify its business. Around 24 August 2006, Mr Shi received a proposal on the potential acquisition by the Company of an interest in Yichun Water Industry Company Limited (“Yichun”), a sino-foreign equity joint venture incorporated in the PRC in which Onfar International Limited (“Onfar”) beneficially owned a 51 per cent equity interest (the “Onfar Project”). Mr Shi also met with the General Manager of Yichun to discuss the prospects of the water supply and sewage treatment industry in the PRC.

On 28 August 2006, Mr Shi introduced the Onfar Project to the Company and reported to, among others, Mr Sze the matters he discussed with the General Manager of Yichun. They also considered the prospects of the water supply and sewage treatment industry in the PRC.

On around 24 or 25 September 2006, Yichun provided to the Company for review a document containing some basic background information on Yichun City and the business operations of Yichun. Between 26 and 29 September 2006, Mr Sze, Mr Shi and another director of the Company visited Yichun City to perform due diligence on the Onfar Project. They also met with the Deputy Managing Director of Yichun during the due diligence exercise.

On 3 October 2006, the Company requested suspension of trading of its shares with effect from 9:30 a.m. on that day pending release of an announcement regarding a discloseable transaction of a price sensitive nature. The Listing Division received a draft announcement in the afternoon disclosing, for the first time, the acquisition by a wholly-owned subsidiary of the Company from Boost Skill Investments Limited (“Boost Skill”) of 40 per cent of the entire issued share capital in Onfar and the shareholder’s loan owing by Onfar to Boost Skill, at an aggregate consideration of HK\$36 million. Upon completion, the Company would indirectly hold a 20.4 per cent interest in Yichun.

The Unusual Trading Movements of the Shares of the Company (the “Shares”)

There were unusual trading movements of the Shares recorded on 8, 14, 18 and 19 September 2006. The price of the Shares increased to a maximum of 32.3 per cent, 33.3 per cent, 21.6 per cent and 33.6 per cent respectively compared to the previous closing price. The trading volume was 10.4 times, 21.9 times, 1.5 times and 3.1 times of the preceding 10-day average and constituted 0.7 per cent, 3.4 per cent, 2.3 per cent and 5.7 per cent of the Company’s issued share capital at the relevant time. Following the enquiries by the Listing Division, the Company issued an announcement on each of those dates in which the directors of the Company confirmed that there were no negotiations or agreements relating to intended acquisitions or realizations which were discloseable under Rule 13.23 of the Exchange Listing Rules, and that they were not aware of any matter discloseable under the general obligation imposed by Rule 13.09 which was or might be of a price sensitive nature (the “Standard Confirmation”).

On 27 September 2006, the price of the Shares increased to a maximum of 40.1 per cent compared to the previous closing price, the trading volume was 1.5 times of the preceding 10-day average and constituted 5.1 per cent of the Company’s issued share capital at the time. In response to the Division’s enquiry, the Company issued an announcement on 27 September 2006 containing the Standard Confirmation (the “First Announcement”).

On 28 September 2006, the price of the Shares increased further to a maximum of 33.3 per cent compared to the previous closing price, the trading volume was 1.9 times of the preceding 10-day average and constituted 7.4 per cent of the Company’s issued share capital at the time. In response to the Division’s enquiry, the Company issued an announcement again on 28 September 2006 containing the Standard Confirmation (the “Second Announcement”).

Rules 13.10, 2.13(2) and 13.09(1) of the Exchange Listing Rules (collectively the “Relevant Rules”)

Rule 13.10 requires an issuer to respond promptly to any enquiries made of the issuer by the Exchange concerning unusual movements in the price and trading volume of its listed securities or any other matters by giving such relevant information as is available to the issuer, or if appropriate, by issuing an announcement clarifying the situation. Note 1 to Rule 13.10 provides that if it is not possible to make such an announcement, for example because negotiations may have reached a delicate stage, a temporary suspension of dealings in the issuer’s securities may be necessary.

The Listing Division alleged that the price and volume movements of the Shares inferred that the information concerning the Company's interest in and possible intention to acquire Onfar/Yichun had been leaked into the market from an unidentified source. The Company's failure to accurately and fully respond to the Division's enquiries by disclosing to the Exchange information relating to the Onfar Project and/or request a temporary suspension of dealings in the Shares in response to the Division's enquiries on 27 and 28 September 2006 constituted a breach of Rule 13.10.

Rule 2.13(2) provides that information contained in any announcement or corporate communication required pursuant to the Exchange Listing Rules must be accurate and complete in all material aspects and not be misleading or deceptive. In complying with this requirement, the issuer must not, among other things, omit material facts of an unfavourable nature or fail to accord them with appropriate significance.

The Listing Division alleged that in failing to disclose in the First Announcement and the Second Announcement (collectively, the Relevant Announcements") information pertaining to the Onfar Project, each of the Relevant Announcements was rendered inaccurate and incomplete as required by Rule 2.13(2).

Rule 13.09(1) requires each issuer to keep the Exchange, members of the issuer and other holders of its listed securities informed as soon as reasonably practicable of any information relating to the group, which among other things, is necessary to enable them and the public to appraise the position of the group or might be reasonably expected to materially affect market activity in and the price of its securities.

The Listing Division alleged that information relating to the Onfar Project, including the Company's conduct of due diligence thereon, was information which might have a material effect on market activity in and the price of the Shares. The Company's failure to disclose information relating to the Onfar Project promptly and/or earlier than 3 October 2006 constituted a breach of Rule 13.09(1).

The Listing Division further alleged that each of Mr Sze and Mr Shi breached the Director's Undertaking.

Decision

The Listing Committee concluded, among other things, that:

1. the Company breached Rules 2.13(2), 13.09(1) and 13.10 of the Exchange Listing Rules;
2. Mr Sze breached the Director's Undertaking in failing to use his best endeavour to procure the Company's compliance with the Relevant Rules; and
3. Mr Shi breached the Director's Undertaking in failing to use his best endeavour to procure the Company's compliance with the Relevant Rules.

The Listing Committee decided to impose a public censure on the Company, Mr Sze and Mr Shi for their respective breaches mentioned above.

The Listing Committee further determined that:

1. the Company should retain an independent professional adviser satisfactory to the Listing Division (the “Adviser”) to conduct a thorough review of and make recommendations to improve the Company’s internal controls for compliance with the disclosure requirements under the Exchange Listing Rules, and to provide the Listing Division with the written report of the Adviser containing recommendations to improve the Company’s internal controls within two months of 27 August 2008;
2. the Company should furnish the Listing Division with the Adviser’s written report on the Company’s full implementation of the Adviser’s recommendations within a further period of two months;
3. the Company should retain the Adviser on an ongoing basis for consultation on compliance with the Exchange Listing Rules for a period of two years from 27 August 2008. The Adviser shall be accountable to the Audit Committee of the Company; and
4. Mr Sze and Mr Shi should undergo training on compliance and corporate governance matters for 24 hours to be given by a recognised professional organisation satisfactory to the Listing Division to be completed within six months from 27 August 2008. The Company should provide the Listing Division with the training provider’s written certification of full compliance with this training requirement by these directors within two weeks after their full compliance with the training requirement.

Mr Luk Chi Shing (“Mr Luk”) was also a member of the Company’s Board of Directors at the material time. However, as he could not be located for service of the documents relating to the disciplinary hearing, the findings of the Listing Committee do not extend to him. The Exchange reserves its right to consider the position of Mr Luk as and when he can be located and served with the relevant documents concerning the disciplinary proceedings.

For the avoidance of doubt, the Exchange confirms that this public censure applies only to the Company, Mr Sze and Mr Shi and not to any other past or present members of the Board of Directors of the Company.

Richard Williams, Head of Listing, commented: “The decision in this case to impose a public sanction on the Company and the two of the executive directors concerned serves as a reminder to issuers of the importance attached by the Exchange to the timely disclosure of information which is accurate and complete. Disclosure to shareholders and the investing public with the objective of placing them in a position to make informed investment decisions is the cornerstone of our regulatory regime.

The primary regulatory message is that a disclosure obligation arises as soon as secrecy concerning a potentially price sensitive development appears to have been lost. All directors of listed issuers are encouraged to consider the guidance provided in “The Guide on Disclosure of Price-sensitive Information” published by the Exchange in January 2002 (the “Guide”), which is accessible from the Exchange’s website. As stated in the Guide, if negotiations or discussions regarding a potentially price-sensitive matter are extended to include more than a small group of people or if it becomes difficult to ensure the confidentiality of the information, an announcement should be made as soon as possible. In this case, the Listing Committee decided that the Company should have disclosed information relating to the Company’s interest in and possible intention to acquire an interest in another company, when it appeared that such information had been leaked into the market and before the terms of the transaction had been finalized.

Another important facet to this case concerns the Company’s failure to accurately and fully respond to the Division’s enquiries made pursuant to Rule 13.10 into unusual trading movements of the Company’s shares. I wish to emphasize that in circumstances where there are prevailing factors which might be relevant to unusual trading movements, the listed issuer and its directors should not be hasty to rule out the significance or relevance of such reasons but should at least, given the wording of the standard Rule 13.10 announcements, inform the Division and make appropriate disclosure of those reasons in response to Rule 13.10 enquiries by the Division. The benchmark is relatively low and issuers and their management are encouraged to adopt a prudent approach to their obligations.

The decision also demonstrate once again that in addition to punishing past misconduct through the imposition of public sanctions the Committee will, where appropriate, seek to encourage enhanced standards of corporate governance and compliance by directing a review of the issuer’s internal controls, improvement on such controls, the appointment of an external compliance adviser and that directors to undergo training on compliance and corporate governance matters. Such remedial measures seek to encourage and promote listing rule compliance and thus seek to prevent further breaches of the Exchange Listing Rules by the issuer and its management going forward.”