



THE STOCK EXCHANGE OF HONG KONG LIMITED

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

10 April 2008

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

- 1. Mudan Automobile Shares Company Limited (the “Company”) (Stock code: 8188);**
- 2. Mr Sun Min Biao, a former executive director of the Company removed on 3 March 2008 (“Mr Sun”);**
- 3. Mr Hou Cheng Bao an executive director of the Company (“Mr Hou”);**
- 4. Mr Yang De Xiang, a former executive director of the Company removed on 3 March 2008 (“Mr Yang”);**
- 5. Mr Shi Jin Cheng, a former executive director of the Company resigned effective 8 October 2004 (“Mr Shi”);**
- 6. Mr Shao Zhi Nan, a former executive director of the Company resigned effective 20 June 2003 (“Mr Shao”);**
- 7. Mr Jiang Wei Sheng, a former executive director of the Company resigned effective 8 October 2004 (“Mr Jiang”); and**
- 8. Mr Xu Hong Bing, a former executive director of the Company resigned effective 22 April 2005 (“Mr Xu”).**

Further, the GEM Listing Committee criticises the following parties for breaching the GEM Listing Rules:

- 1. Madam You Lian Qun, a former non-executive director of the Company resigned effective 8 October 2004 (“Madam You”);**
- 2. Mr Zhang Xiao Yu, a former independent non-executive director of the Company resigned effective 30 June 2004 (“Mr Zhang”); and**
- 3. Mr Wu Chang Fa, a former independent non-executive director of the Company resigned effective 30 June 2004 (“Mr Wu”).**

On 18 December 2007, the GEM Listing Committee conducted a hearing into the conduct of the Company, Mr Sun, Mr Hou, Mr Yang, Mr Shi, Mr Shao, Mr Jiang, Mr Xu, Madam You, Mr Zhang and Mr Wu (collectively, the “Relevant Directors”) in relation to the obligations under the GEM Listing Rules and the Director’s Declaration, Undertaking and Acknowledgement given by a director of PRC issuer to the Exchange in the form set out in Appendix 6 Form B to the GEM Listing Rules (the “Director’s Undertaking”).

Facts

By an announcement dated 22 June 2006

(<http://gem.ednews.hk/listedco/listconews/gem/20060623/GLN20060623011.pdf>), the Company disclosed the following continuing connected transactions conducted between 2002 and 2004:

- A. Transactions with Jiangsu Mudan Automobile Group Company Limited (“JM”), a promoter, substantial shareholder and connected person of the Company:
- (a) the Company and JM used their respective bank credit lines to transfer money to each other;
 - (b) the Company and JM paid for the purchases of raw materials on behalf of each other;
 - (c) the Company and JM made payments on behalf of each other of certain expenses such as contributions made to the pension fund and social security fund;
 - (d) the Company and JM made direct advances to each other;
 - (e) the Company and JM sold cars on behalf of each other and received sales proceeds respectively. This group of payments also captured the payments where customers confused the two companies and remitted payments to the wrong company and which had not been diverted back to the rightful owner; and
 - (f) JM sold some chassis to the Company in 2004 of which 34 were later found defective and returned to JM. JM was obliged to refund the Company for the chassis returned. However, the entire sum remained outstanding as at 31 December 2004.

No written agreement was entered into between the Company and JM regarding the payments or arrangements in (a), (b), (c), (d) and (e). The net outstanding balance owed by JM to the Company as at 31 December 2004 was RMB203,176,037 which was interest-free without fixed terms of repayment and unsecured.

The Listing Division alleged that the Company breached: (i) the then Rule 20.50 and Rule 20.63 for failing to comply with the reporting, announcement and independent shareholders’ approval requirements in respect of payments made by the Company to, on behalf of or for the benefit of JM which constituted financial assistance granted by the Company to JM. Such financial assistance was not provided in the ordinary and usual course of the business of the Company or on normal commercial terms; (ii) Rule 17.15 for failing to disclose by a press announcement the sums due to the Company arising from the connected transactions with JM when the aggregate sum due exceeded 25 per cent of the Company’s relevant net asset value before 31 March 2004 or the 8 per cent threshold from 31 March 2004; and (iii) Rule 17.22 for failing to disclose the amount due from JM as at half yearly, quarterly period end or year end in the Company’s quarterly and interim accounts of 2002 to 2004 and annual accounts of 2002 and 2003.

B. Transactions with Zhangjiagang Jishun Transportation Industrial Co., Ltd. (“ZJTI”), an associate of JM and a connected person of the Company

The Company purchased raw materials from ZJTI and sold steel to ZJTI. The amount due from the Company to ZJTI for the purchase of raw materials in 2002, 2003 and 2004 were RMB6,534,848, RMB12,602,861 and RMB16,540,245 respectively. The amount due from ZJTI to the Company for the sale of steel in 2002, 2003 and 2004 were RMB12,829,835, RMB19,833,911 and RMB13,437,900 respectively.

The Division alleged that the Company breached the then Rules 20.34, 20.35 and 20.36 and Rules 20.47 and 20.48 for failing to comply with the reporting, announcement and independent shareholders’ approval requirements in respect of the continuing connected transactions with ZJTI which were not on normal commercial terms.

C. Transactions with Zhangjiagang Mudan Bus Parts Co., Ltd. (“ZMBPC”), a promoter and connected person of the Company

The Company sold scrap materials to ZMBPC in 2004 which amounted to RMB1,525,673. Such sales were made continuously throughout the year pursuant to agreements executed between the parties in each quarter of the year.

The Division alleged that the Company breached Rule 20.47 for failing to comply with the announcement requirement.

Further, the Division alleged that: (i) each of the Relevant Directors breached the Director’s Undertaking; and (ii) Mr Shao and Mr Xu failed to perform their duties as Compliance Officers as required under the then Rule 5.15 and Rule 5.20 for failing to advise and assist the Board in implementing procedures to ensure the Company’s compliance with the GEM Listing Rules.

Decision

The GEM Listing Committee concluded that:

- (i) the Company breached the then Rules 20.34, 20.35, 20.36, 20.50, 17.15 and Rule 17.22 of the GEM Listing Rules for transactions conducted between 2002 and 30 March 2004 and Rules 20.47, 20.48, 20.63, 17.15 and 17.22 of the GEM Listing Rules for transactions conducted between 31 March 2004 and 31 December 2004;
- (ii) each of the Relevant Directors breached the Director’s Undertaking to use his or her best endeavours to cause the Company to comply with the GEM Listing Rules;
- (iii) the breach of the Director’s Undertaking committed by Mr Sun was persistent;
- (iv) the retention of office by Mr Sun is prejudicial to the interests of investors;

- (v) Mr Shao breached the then Rule 5.15 of the GEM Listing Rules; and
- (vi) Mr Xu breached the then Rule 5.15 and Rule 5.20 of the GEM Listing Rules.

The GEM Listing Committee decided to impose the following sanctions on the parties:

- a public censure on the Company, Mr Sun, Mr Hou, Mr Yang, Mr Shi, Mr Shao, Mr Jiang and Mr Xu for their respective breaches mentioned in (i), (ii), (v) and (vi) above; and
- a public statement which involves criticism on Madam You, Mr Zhang and Mr Wu for their breaches mentioned in (ii) above.

The GEM Listing Committee further directed that:

1. the Company 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: (i) GEM Listing Rules compliance in relation to connected transactions in particular transactions with JM and its subsidiaries; (ii) management of directors’ potential or actual conflict of interests; (iii) maintaining proper books, records and accounts; and (iv) ensuring due process and the Company’s autonomy in its operation, management and actions required in compliance with the GEM Listing Rules and provide the Listing Division with the written report of the Adviser within two months of 10 April 2008;
2. the Company 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 appoint a Compliance Adviser satisfactory to the Listing Division to provide guidance to the Company on compliance matters for a period for two years, the appointment to be made within one month after 10 April 2008;
4. Mr Hou undergo not less than 24 hours of training in compliance and corporate governance matters on courses held by the Hong Kong Institute of Directors or another recognised institute acceptable to the Listing Division; such training to be completed within six months from 10 April 2008 and evidence of completion be furnished to the Listing Division forthwith; and
5. as a pre-requisite to any future appointment(s) as a director of any company listed on the Exchange of each of Mr Sun, Mr Yang, Mr Shi, Mr Shao, Mr Jiang, Mr Xu, Madam You, Mr Zhang and Mr Wu, each of them must first obtain training on GEM Listing Rules compliance, for a minimum of 24 hours; such training should be provided by training provider(s) acceptable to the Listing Division and evidence of completion of training to be furnished to the Listing Division.

The GEM Listing Committee was minded to impose a public statement under Rule 3.10(7) of the GEM Listing Rules on Mr Sun that in the Exchange's opinion, the retention of office by Mr Sun is prejudicial to the interests of investors by reason of his persistent failure to discharge his responsibilities under the Director's Undertaking. However, in light of the fact that Mr Sun was removed from his directorship on 3 March 2008, the GEM Listing Committee is of the view that imposition of such sanction on Mr Sun is no longer necessary.

Richard Williams, Head of Listing, said, "The decision in this case is based on a large number of serious breaches which took place over a number of years. In addition to the disciplinary action taken by the Exchange the Company has been and remains suspended from trading.

There are a number of strands to this decision which merit commentary.

Public sanctions have been imposed on both the Executive and Non-Executive members and former members of the board of directors. The rules make it plain that responsibility for compliance has at its root a collective responsibility on all members of the board. It is of vital importance that all members of the board of directors ensure that in accepting office they have the requisite knowledge of the rules to enable them to discharge their compliance responsibilities to shareholders, the Exchange and the market. In appropriate circumstances, while acknowledging the differing roles of directors within the corporate structure of a listed company, non-executive (including those considered to be independent) directors are potentially liable for public sanction if, during their tenure of office, they have acted or failed to act in such a way that they are not considered to have discharged their obligations under the undertaking they have given to the Exchange.

The rules require the appointment of an executive director as a compliance officer who has specific and defined responsibilities in the area of compliance. This requirement has particular importance in the case of GEM companies and it is incumbent on the holder of this office to ensure that he equips himself with the requisite knowledge to enable him to discharge the obligation and where he is unsure take professional advice or consult the Exchange. As in this case, public sanctions may follow if the incumbent fails in his duties and responsibilities.

It has been a consistent theme of the commentaries I have made on disciplinary decisions to emphasize the need and importance of a listed company establishing and maintaining adequate internal controls and systems by which compliance with listing rule obligations can be achieved. The failure to have in place adequate systems and controls appears to have been a major contributing factor in the commission of the breaches described in this case. In this case the Listing Committee has under its powers to direct remedial action required that a wide range of steps be taken towards improving the Company's corporate governance. These steps include the appointment of an external compliance adviser and training requirements for directors (and former directors). Similar action will no doubt be directed by the Committee in any cases highlighting issues of the same character brought before it."