

香港聯合交易所有限公司

(香港交易及結算所有限公司全資附屬公司)

THE STOCK EXCHANGE OF HONG KONG LIMITED

(A wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited)

A listed issuer’s disclosure of its financial information by way of periodic results announcements and reports is an important piece of information necessary for the shareholders and investors to appraise the listed issuer’s performance and future prospect, and to make their investment decisions. It is important that such disclosure contains accurate and complete information in all material respects, and not misleading or deceptive.

The implementation of adequate and effective risk management and internal control systems is vital as those systems affect the listed issuer’s ability to comply with the Exchange Listing Rules.

Directors must read, understand and focus on the contents of such disclosure, and take all reasonable steps to ensure that the financial information to be disclosed is accurate. They must also follow up anything untoward that comes to their attention.

Directors must review the contribution and ability required of each director in order for him to be able to discharge his director’s duties and responsibilities.

The Listing Committee of The Stock Exchange of Hong Kong Limited (“Listing Committee”)

CENSURES:

- (1) **Shandong Molong Petroleum Machinery Company Limited (“Company”)** (Stock Code: 568)

for breaching Rules 2.13(2) of the *Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited* (“**Exchange Listing Rules**”) for failing to ensure that the Company’s financial information contained in the following disclosures was accurate and complete in all material respects, and not misleading or deceptive (“**Disclosure Issue**”):

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- (a) the Company's announcement of 24 April 2015 in relation to its first quarterly results for the three months ended 31 March 2015;
- (b) the Company's announcement of 28 August 2015 in relation to its interim results for the six months ended 30 June 2015;
- (c) the Company's interim report for the six months ended 30 June 2015, published on 29 September 2015;
- (d) the Company's announcement of 30 October 2015 in relation to its third quarterly results for the nine months ended 30 September 2015, which contained a profit forecast for 2015 ("**2015 Profit Forecast**");

((a) to (d) above are collectively referred to as "**2015 Disclosure**")

- (e) the Company's announcement of 28 April 2016 in relation to its first quarterly results for the three months ended 31 March 2016;
- (f) the Company's announcement of 19 August 2016 in relation to its interim results for the six months ended 30 June 2016;
- (g) the Company's interim report for the six months ended 30 June 2016, published on 28 September 2016;
- (h) the Company's announcement of 26 October 2016 in relation to its third quarterly results for the nine months ended 30 September 2016, which contained a profit forecast for 2016 ("**2016 Profit Forecast**"),

((e) to (h) above are collectively referred to as "**2016 Disclosure**")

AND CENSURES:

- (2) **Mr Zhang En Rong**, former executive director ("**ED**") and Chairman of the Company ("**Mr ER Zhang**");
- (3) **Mr Zhang Yun San**, former ED and Deputy Chairman of the Company ("**Mr YS Zhang**");

- (4) **Mr Yang Jin**, former ED and chief financial officer (“**CFO**”) of the Company (“**Mr Yang**”);
- (5) **Mr Guo Huan Ran**, former ED and Chairman of the Company (“**Mr HR Guo**”);
- (6) **Mr Guo Hong Li**, former non-executive director (“**NED**”) of the Company (“**Mr HL Guo**”);
- (7) **Ms Wang Chun Hua**, former NED and independent non-executive director (“**INED**”) of the Company (“**Ms Wang**”);
- (8) **Mr Lin Fu Long**, former ED of the Company (“**Mr Lin**”),

AND CRITICISES:

- (9) **Mr John Paul Cameron**, former INED of the Company (“**Mr Cameron**”);

for breaching their obligations under:

- (a) Rule 3.08(a) (in respect of Mr ER Zhang, Mr YS Zhang and Mr Yang only) and Rule 3.08(f); and
- (b) the *Declaration and Undertaking with regard to Directors of an Issuer incorporated in the People’s Republic of China (“PRC”)* given to the Exchange in the form set out in Appendix 5H to the Exchange Listing Rules (“**Director’s Undertaking**”) for failing to comply to the best of their ability with the Exchange Listing Rules and the applicable laws and rules of the PRC, and to use their best endeavours to procure the Company’s compliance with the Exchange Listing Rules,

AND CRITICISES:

- (10) **Mr Xiao Qing Zhou**, former NED of the Company (“**Mr Xiao**”);
- (11) **Mr Qin Xue Chang**, former INED of the Company (“**Mr Qin**”),

for breaching their obligations under the Director’s Undertaking for failing to comply to the best of their ability with the applicable laws and rules of the PRC, and to use their best endeavours to put in place procedures for proper and adequate reporting of the Company’s affairs and operations to Mr ER Zhang, so as to enable him to discharge his director’s duties,

(the directors identified at (2) to (11) above are collectively referred to as “**Relevant Directors**”),

AND CENSURES:

- (12) **Mr Zhang Jiu Li**, former supervisor of the Company (“**Mr JL Zhang**”);
- (13) **Mr Hao Liang**, former supervisor of the Company (“**Mr Hao**”); and
- (14) **Mr Fan Ren Yi**, former supervisor of the Company (“**Mr Fan**”),

for breaching their obligations under the *Declaration and Undertaking with regard to Supervisors of an Issuer incorporated in the PRC* given to the Exchange in the form set out in Appendix 5I to the Exchange Listing Rules (“**Supervisor’s Undertaking**”) for failing to comply to the best of their ability with the applicable laws and rules of the PRC and to use their best endeavours to procure the Company and the Relevant Directors’ compliance with the Exchange Listing Rules,

(the supervisors identified at (12) to (14) above are collectively referred to as “**Relevant Supervisors**”).

For the avoidance of doubt, the Exchange confirms that the sanctions and directions in this news release apply only to the Company, the Relevant Directors and the Relevant Supervisors, and not to any other past or present members of the board of directors or supervisors of the Company.

HEARING

On 3 July 2019, the Listing Committee conducted a hearing into the conduct of the Company, the Relevant Directors and the Relevant Supervisors in relation to their obligations under the Exchange Listing Rules, the Director’s Undertakings and the Supervisor’s Undertakings.

BACKGROUND

The Company is principally engaged in energy equipment industry for product research and development, production and sales. It is also listed on the Small and Medium-sized Enterprises Board of the Shenzhen Stock Exchange (stock code 2490).

Mr ER Zhang and Mr YS Zhang are founders of the Company. Mr Yang was appointed as the Company’s CFO in March 2012 prior to his appointment as ED of the Company on 29 June 2016.

Disclosure Issue

The Relevant Directors and the Relevant Supervisors (to the extent of their tenure) approved and confirmed the accuracy and completeness of each set of financial information disclosed in the 2015 and 2016 Disclosures, including the 2015 and 2016 Profit Forecasts.

The Company made various revisions to the Company's 2015 and 2016 Disclosures (see the Company's announcements of 30 March 2017, 29 September 2017 and 2 October 2017). The 2015 and 2016 Disclosures were inaccurate. The discrepancies between the actual amounts and the financial information contained in the 2015 Disclosure ("**2015 Discrepancies**") and 2016 Disclosure were significant.

The China Securities Regulatory Commission ("**CSRC**") found the Company, the Relevant Directors and the Relevant Supervisors to be in breach of the Securities Law of the PRC by reason of the false records contained in the 2015 and 2016 Disclosures.

The Shenzhen Stock Exchange found the Company, Mr ER Zhang, Mr YS Zhang, Mr Yang, Mr HR Guo, Mr HL Guo, Ms Wang, Mr Hao and Mr JL Zhang to be in breach of its rules by reason of, among others, the material accounting errors in the 2016 Disclosure, and the material deficiency in the Company's internal controls.

The Company submitted that it discovered the incorrect information on or about 22 March 2017, after the commencement of the CSRC's investigation. It gave two explanations for its disclosure of the relevant incorrect financial information:

- (a) First explanation – provisional adjustments ("**Provisional Adjustments**") were made to the quarterly results for ensuring its financial stability. The relevant adjustments were procured by Mr YS Zhang and Mr Yang.
- (b) Second explanation – the finance staff responsible for estimating and recording the revenue and costs did not understand the market prices sufficiently, which resulted in the material differences between the estimated and the actual amounts.

The Department did not assert a Rule 3.08 breach by Mr Xiao and Mr Qin in relation to the Disclosure Issue. In respect of Mr Xiao, he ceased to be the Company's director on 7 September 2015. The Department accepted that, prior to the revision of the 2015 Profit Forecast in or around the end of January 2016, Mr Xiao would not have been alerted to any of the 2015 Discrepancies or possible internal control deficiencies. In respect of Mr Qin, there was evidence that Mr Qin had raised questions and comments about the accuracy of some of the 2015 and 2016 financial data, and that he suggested the Company engaging an independent auditor to review the 2016 interim and quarterly results, and recommended enhancement to training and internal controls around the time when the 2015 annual results were published.

Internal controls

The Company acknowledged that for the first three quarters of 2016, the Company did not conduct effective audit and control on the recognition and measurement of some operational revenue and the carrying forward of operational costs. This led to material misstatement in the financial statements.

Delegation Issue

Mr ER Zhang did not attend the office between 2005 and February 2017 and delegated his responsibilities to his son, Mr YS Zhang (“**Delegation Issue**”). He only attended Board meetings by teleconference. No one reported to Mr ER Zhang anything about the Company’s operations or financial performance, apart from provision of its quarterly, interim and annual results to him.

Apart from Mr Cameron who asserted that he was not aware of the Delegation Issue, the other Relevant Directors believed that Mr ER Zhang had discharged his obligations.

EXCHANGE LISTING RULES

Company

Rule 2.13(2) requires an issuer to ensure that the information contained in any announcement or corporate communication required pursuant to the Exchange Listing Rules is accurate and complete in all material respects and not misleading or deceptive.

Directors

Under Rules 3.08, 3.16 and 13.04 of the Exchange Listing Rules, the Board is collectively responsible for the Company’s management and operations, and the directors are collectively and individually responsible for ensuring the Company’s full compliance with the Exchange Listing Rules.

Rule 3.08 provides that the Exchange expects directors, both collectively and individually, to fulfil fiduciary duties and duties of skill, care and diligence to a standard at least commensurate with the standard established by Hong Kong law. These duties include a duty to act honestly and in good faith in the interests of the issuer as a whole (Rule 3.08(a)), and to apply such degree of skill, care and diligence as may reasonably be expected of a person of his/her knowledge and experience and holding his office within the issuer (Rule 3.08(f)).

Rule 3.08(f) highlights the importance of directors taking an active interest in the issuer’s affairs and having a general understanding of its business. It provides that “[d]irectors must satisfy the required levels of skill, care and diligence. Delegating their functions is permissible but does not absolve them from their responsibilities or from applying the required levels of skill, care and diligence. Directors do not satisfy these required levels if they pay attention to the issuer’s affairs only at formal meetings. At a minimum, they must take an active interest in the issuer’s affairs and obtain a general understanding of its business. They must follow up anything untoward that comes to their attention”.

A director of a listed issuer incorporated in the PRC is under an obligation, pursuant to his Director’s Undertaking, to:

- (a) comply to the best of his ability with the Exchange Listing Rules and all applicable the laws and rules from time to time in force in the PRC relating to the governing, operation, conduct or regulation of public companies in the PRC or elsewhere; and
- (b) use his best endeavours to procure the Company's compliance with the Exchange Listing Rules.

Under the Corporate Governance Code and Corporate Governance Report ("**CG Code**"), Appendix 14 to the Exchange Listing Rules, directors are required, among others, to ensure:

- (a) that the Company's risk management and internal control systems are reviewed by the Board on an ongoing basis, and when conducting their annual review, the directors should consider the effectiveness of the Company's processes for financial reporting and Exchange Listing Rule compliance (code provisions C.2.1 and C.2.3 of the CG Code);
- (b) the adequacy of resources, staff qualifications and experience (code provision C.2.2 of the CG Code); and
- (c) that, as part of their assessment of the adequacy and effectiveness of the Company's risk management system, the directors regularly review the contribution required from a director to perform his responsibilities to the Company, and whether he is spending sufficient time performing them (principle A.1 of the CG Code).

Supervisors

A supervisor of a listed issuer incorporated in the PRC is under an obligation, pursuant to his Supervisor's Undertaking, to:

- (a) comply to the best of his ability with all applicable the laws and rules from time to time in force in the PRC relating to the responsibilities of supervisors in connection with the governing, operation, conduct or regulation of public companies in the PRC or elsewhere; and
- (b) use his best endeavours to procure the Company and the directors' compliance with the Exchange Listing Rules.

Under their Terms of Reference, the Supervisors are required to review and audit the Company's regular/interim reports and provide their audit report, and supervise the conduct of the Directors and senior management in relation to their management of the Company.

LISTING COMMITTEE'S FINDINGS OF BREACH

The Listing Committee considered the written and/or oral submissions of the Listing Department, the Company, the Relevant Directors and the Relevant Supervisors, and concluded as follows:

Company's breaches and its risk management and internal control deficiencies

The Listing Committee found that the Company:

- (a) was in breach of Rule 2.13(2). The 2015 and 2016 Disclosures were not only misleading but deceptive; and
- (b) did not maintain adequate and effective risk management and internal control systems to ensure that the 2015 and 2016 Disclosures complied with Rule 2.13(2), and to enable Mr ER Zhang's proper discharge of his director's duties.

Relevant Directors' breaches

The Listing Committee found the following breaches by the Relevant Directors:

Breach	Director
Rule 3.08(a)	
<p>Failure to act honestly and in good faith in the interests of the Company as a whole.</p> <p>Mr ER Zhang had no knowledge about the Company's operations and yet he approved the 2015 and 2016 Disclosures.</p> <p>Mr YS Zhang and Mr Yang were aware of the provisional adjustments made to the financial results for the first three quarters of 2015 and 2016, but chose to approve the incorrect 2015 and 2016 Disclosures.</p>	<p>Mr ER Zhang Mr YS Zhang Mr Yang</p>
Rule 3.08(f)	
<p>Failure to ensure that the Company had adequate and effective risk management and internal control systems for compliance with Rule 2.13(2).</p>	<p>Mr ER Zhang Mr YS Zhang Mr Yang Mr HR Guo Mr HL Guo Ms Wang Mr Lin Mr Cameron</p>

<p>There was serious weakness in the Company's corporate governance in relation to the Delegation Issue. There was no evidence that the Director took any steps to ensure that there were proper reporting procedures of the Company's affairs to Mr ER Zhang, or review Mr ER Zhang's contribution and ability to perform his responsibilities to the Company, and whether he was spending sufficient time performing them.</p>	<p>Mr ER Zhang Mr YS Zhang Mr Yang Mr HR Guo Mr HL Guo Ms Wang Mr Lin</p>
<p>A director should have a questioning mind when red flags were raised by way of the 2015 Discrepancies. The director did not make any enquiries or consider whether there were any internal control implications given the significant 2015 Discrepancies.</p>	<p>Mr ER Zhang Mr YS Zhang Mr HR Guo Mr HL Guo Ms Wang</p>
<p>At the time when the Company revised the 2015 Profit Forecast, and later when reviewing and approving the 2015 annual results, the director should have discovered the significant 2015 Discrepancies. However, there was no evidence that he/she made any enquiries as to what had caused the discrepancies; considered whether there were any risk management and internal control deficiencies, or how to address such deficiencies; or considered whether there were any Exchange Listing Rule implications, namely whether the Company's 2015 Disclosure was accurate and complete.</p>	<p>Mr Lin Mr Cameron</p>
<p><i>Director's Undertaking</i></p>	
<p>Breach of the Director's Undertaking by reason of the breach of Rules 3.08(a) (for Mr ER Zhang, Mr YS Zhang and Mr Yang only) and 3.08(f), and the findings of the CSRC and/or the Shenzhen Stock Exchange against him/her, and for his/her failure to use best endeavours to procure the Company's compliance with Rule 2.13(2) and to maintain adequate risk management and internal controls.</p>	<p>Mr ER Zhang Mr YS Zhang Mr Yang Mr HR Guo Mr HL Guo Ms Wang Mr Lin Mr Cameron</p>
<p><i>Director's Undertaking</i></p>	
<p>Breach of the Director's Undertaking by reason of the findings of the CSRC, and for their failure to use best endeavours to put in place procedures for proper and adequate reporting of the Company's affairs and operations to Mr ER Zhang, so as to enable him to discharge his director's duties.</p>	<p>Mr Xiao Mr Qin</p>

Mr ER Zhang - wilful or persistent disregard of the Listing Rules

The Listing Committee found that Mr ER Zhang willfully and persistently failed to discharge his responsibilities as ED and Chairman under the Exchange Listing Rules for a prolonged period (between 2005 and February 2017).

Breach of Supervisor's Undertaking

The Listing Committee concluded that the Relevant Supervisors breached their Supervisor's Undertakings by reason of:

- (a) the findings made by the CSRC and/or the Shenzhen Stock Exchange; and
- (b) their failure to use their best endeavours to procure the Company and the Relevant Directors' compliance with the Exchange Listing Rules and to maintain adequate risk management and internal controls in relation to the Disclosure and Delegation Issues.

REGULATORY CONCERN

Disclosure underpins the maintenance of a fair and orderly market for the trading of securities in Hong Kong. A listed issuer's disclosure of its financial information by way of periodic results announcements and reports is an important piece of information necessary for the shareholders and investors to appraise the listed issuer's performance and future prospect, and to make their investment decisions.

Rule 2.13 prescribes the Exchange's expectation of the requirements of listed issuers' corporate communications. The implementation of adequate and effective risk management and internal control systems is vital as those systems affect the listed issuer's ability to comply with the Exchange Listing Rules. Delegation of responsibility to a director or other staff does not absolve other directors individually or collectively from taking all reasonable steps to monitor the execution of the delegated task, and to take prompt and effective remedial action where deficiencies in execution are noted.

Given the nature and importance of a listed issuer's disclosure of its financial information, its directors must read, understand and focus on the contents of such disclosure, and they must take all reasonable steps to ensure that the financial information to be disclosed is accurate. Where necessary, the directors must make further enquiries and follow up on anything untoward that comes to their attention. In relation to reliance on external advisor's advice, the directors should have a questioning mind and employed his own wisdom and experience to weigh that advice, particularly where are any red flags.

The Listing Committee considered that the breaches and the conduct in question are serious. The conduct in this case, by reference to the magnitude of the incorrect and misleading/deceptive financial information and the period during which the investors traded on such information, damaged the integrity of the market.

This case reveals the Company had serious corporate governance issues in relation to Mr ER Zhang's delegation of his responsibilities to Mr YS Zhang between 2005 and February 2017, during which period Mr ER Zhang remained the Company's ED and Chairman. The duties owed by a director to the Company are not to be taken lightly. Unless the director, the board and the listed issuer are satisfied that the relevant director can devote sufficient time and attention required of him in due performance of his director's duties, he should resign. A director does not satisfy the required levels of skill, care and diligence if he pays attention to the issuer's affairs only at formal meetings.

SANCTIONS

Having made the findings of breach stated above, the Listing Committee decides to impose:

- (1) a public censure against the Company for its breach of Rule 2.13(2);
- (2) a public censure against each of Mr ER Zhang, Mr YS Zhang, Mr Yang, Mr HR Guo, Mr HL Guo, Ms Wang, Mr Lin, Mr JL Zhang, Mr Hao and Mr Fan. In relation to Mr ER Zhang, in the Exchange's opinion, had he remained as director of the Company, his retention of office would have been prejudicial to the interests of the investors;
- (3) a public statement involving criticism against each of Mr Cameron, Mr Xiao and Mr Qin.

The Committee further directed:

- (4) the Company to: (a) appoint an independent Compliance Adviser (as defined in Rule 3A.01 namely, any corporation or authorised financial institution licensed or registered under the Securities and Futures Ordinance for Type 6 regulated activity and permitted under its licence or certificate of registration to undertake work as a sponsor and, as applicable, which is appointed under Rule 3A.19 or Rule 3A.20 to undertake work as a Compliance Adviser) satisfactory to the Listing Department on an ongoing basis for consultation on Exchange Listing Rule compliance for two years within four weeks from the publication of this news release; and (b) submit the proposed scope of retainer to the Listing Department for comment before appointment of the Compliance Adviser. The Compliance Adviser shall be accountable to the Audit Committee of the Company;

- (5) the Company to: (a) retain an independent professional adviser satisfactory to the Listing Department (“**Adviser**”) to conduct a thorough review of and make recommendations to improve the Company’s internal controls to ensure compliance with the Exchange Listing Rules, within two weeks from the date of publication of this news release. The Company shall provide the Listing Department with the written report of the Adviser containing such recommendations within two months from the publication of this news release. The Company is to submit the proposed scope of retainer to the Listing Department for comment before appointment of the Adviser; and (b) furnish the Listing Department with the Adviser’s written report on the Company’s full implementation of the Adviser’s recommendations within a further period of two months;
- (6) as a pre-requisite of any future appointment as a director of any company listed/to be listed on the Exchange, Mr ER Zhang, Mr YS Zhang, Mr Yang, Mr HR Guo, Mr HL Guo, Ms Wang, Mr Lin, Mr Cameron, Mr Xiao and Mr Qin, who are not currently a director of any other company listed on the Exchange, (a) to attend 24 hours of training (“**Training**”) on Exchange Listing Rule compliance and director’s duties, including 4 hours of training on the financial reporting obligations under the Exchange Listing Rules and 4 hours of training on director’s obligations on the issuer’s risk management and internal control system, to be provided by institutions such as the Hong Kong Institute of Chartered Secretaries, the Hong Kong Institute of Directors or other course providers approved by the Listing Department. The Training is to be completed before the effective date of any such appointment; and (b) to provide the Listing Department with the Training provider’s written certification of full compliance;
- (7) the Company to publish an announcement to confirm that each of the directions in paragraphs (4)(a), (5)(a) and (5)(b) above has been fully complied with within two weeks after the fulfilment of that direction;
- (8) the Company to submit drafts of the announcements referred to in paragraph (7) above for the Listing Department’s comment and may only publish the announcements after the Listing Department has confirmed it has no further comment on them; and
- (9) following the publication of this news release, any changes necessary and any administrative matters which may emerge in the management and operation of any of the directions set out in paragraphs (4) to (8) above are to be directed to the Listing Department for consideration and approval. The Listing Department should refer any matters of concern to the Listing Committee for determination.