



**GUANGDONG KELON ELECTRICAL HOLDINGS COMPANY LIMITED**  
**廣東科龍電器股份有限公司**

*(A joint stock limited company incorporated in the People's Republic of China with limited liability)*  
(Stock Code: 0921)

**ANNOUNCEMENT IN RELATION TO ADMINISTRATIVE SANCTIONS IMPOSED  
BY THE CHINA SECURITIES AND REGULATORY COMMISSION**

Reference is made to the announcement of Guangdong Kelon Electrical Holdings Company Limited (the "Company") dated 20 October 2005 in relation to the receipt by the Company of an Advance Notice of Administrative Penalty (行政處罰事先通知書) from the China Securities Regulatory Commission (the "CSRC") on 17 October 2005, in which the Company also confirmed that it has not received any official document from the CSRC in this regard. The Company would like to inform its shareholders that the Company received a Notice of Decision on Administrative Sanction CSRC (Zheng Jian Fa Zi [2006] No.16) on 4 July 2006, which is summarised as follows (all amounts referred to below are denominated in Renminbi):

**I. INSTANCES OF BREACH**

Investigation results show the following instances of breach, including the use of false records and substantial omissions from the annual reports for 2002, 2003 and 2004 as disclosed by the Company:

A. From 2002 to 2004, the Company prepared false financial reports by overstating revenue from principal operations, understating provision for bad debts and understating damages for legal proceedings, resulting in an overstated profit of RMB119,963,100, RMB118,470,500 and RMB148,759,100 respectively, in the 2002 annual report, the 2003 annual report and the 2004 annual report.

(1) From 2002 to 2004, the Company overstated its revenue and profits from principal operations by issuing invoices for goods which had not yet been sold and by selling invoices and recognising the proceeds of such sales as income.

1. In the 2002 annual report, revenue was overstated in the amount of RMB403,305,400 and profit was overstated in the amount of RMB119,963,100;
2. In the 2003 annual report, revenue was overstated in the amount of RMB304,838,600 and profit was overstated in the amount of RMB89,350,600; and
3. In the 2004 annual report, revenue was overstated in the amount of RMB512,702,900 and profit was overstated in the amount of RMB120,420,500.

(2) From 2003 to 2004, the Company overstated the profit in its annual report by pretending to have sold scrap materials to Zhuhai Defa Air-Conditioner Parts Company Ltd. (珠海德發空調配件有限公司) and Zhuhai Jiangjia Coolant Facility Company Ltd (珠海隆加製冷設備有限公司).

1. In the 2003 annual report, profit was overstated by RMB20,025,200; and
2. In the 2004 annual report, profit was overstated by RMB28,338,600.

- (3) The Company inflated its profits in the annual report through the under-provision for bad debts in 2003

The Company consolidated and made an aging analysis between the balance of accounts receivables due from Guangzhou City Zhuhai District Tengyau Electrical Appliances Co., Ltd. (廣州市海珠區騰遙電器有限公司) in an amount of RMB1,221,400 and the balance of account receivables due from Dongguan City Fumen Supply Yuehua Household Appliances Co., Ltd. (東莞市虎門供銷社粵華家電公司) of RMB-4,721,000 for the year ended 2003, and under-provided for bad debts of accounts receivable due from Guangzhou City Zhuhai District Tengyau Electrical Appliances Co., Ltd. of RMB1,221,400. The Company consolidated and made an aging analysis between the balance of accounts receivable due from Shenzhen City Xinchuyuan Electrical Appliances Co., Ltd. (深圳市新楚源電器有限公司) of RMB4,764,600 and the balance of accounts receivable due from Dianbaixian Shuidong Yuandong Household Appliances Plaza (電白縣水東遠東家電商場) of RMB511,900 for the year ended 2003, where mistakes were made in categorising some of the ages of debts, resulting in the under-provision for accounts receivable due from Shenzhen City Xinchuyuan Electrical Appliances Co., Ltd. of RMB701,400. The Company classified all the accounts receivable due from Shunde City Longyong Metals Jiaodian Co., Ltd. (順德市龍湧五金交電有限公司) which are over one year old as less than three months old, resulting in the under-provision for bad debts of RMB2,629,700. The Company classified all the balances of accounts receivable due from Daqing Seawave Materials Trading Company (大慶海浪物資貿易公司) as less than three months old, resulting in the under-provision for bad debts of RMB603,000. The conducts mentioned above resulted in the inflation of profits of RMB5,155,500 in the 2003 annual report of the Company.

- (4) The Company inflated its profits in the annual report through the under-calculation of litigation damages in 2003

From 10 December to 16 December 2003, the Intermediate People's Court of Foshan City made a series of final judgments in respect of contractual disputes between the Company and certain of its employees, ordering the Company to pay living allowances and litigation costs, etc, of RMB3,939,200 in total to 227 employees. The Company failed to record such amount into the profit and loss account in 2003. The conducts mentioned above resulted in the inflation of profits of RMB3,939,200.

- (B) There are material misstatements in the cash flow statements in 2003 annual report of the Company

In 2003, the Company arranged the sales and purchase of products among the Company and its subsidiaries and issued banker's acceptances and trade acceptances based on this trading background so as to sell to banks for immediate payment and thus obtained a large amount of cash. The cash flow statements of the Company did not truly reflect the aforesaid cash flows. As calculated, in the cash flow statements in the 2003 annual report of the Company, cash from borrowings was understated by RMB3,025,500,000, cash paid to service debts was understated by RMB2,135,730,000 and net cash flow from operating activities was overstated by RMB889,760,000.

- (C) During 2002 to 2004, the Company did not disclose material events such as the change of accounting policies and connected transactions\* with connected parties\* such as joint investment and purchase of goods etc.

- (1) The change of accounting policy on maintenance deposit was not disclosed in 2002 annual report of the Company

In September 2002, the Company changed its accounting policy on maintenance deposit. The Company did not disclose the content, reason and effect of the change of account policy in the 2002 annual report.

- (2) The Company did not perform its obligations of reporting and announcement regarding the material event that Guangdong Greencool Enterprise Development Company Limited (formerly known as Shunde Greencool Enterprise Development Company Limited, hereafter referred to as Guangdong Greencool) (廣東格林柯爾企業發展有限公司(原順德格林柯爾企業發展有限公司, 以下簡稱廣東格林柯爾)) had held shares of the Company. The Company also did not disclose this material event in 2004 annual report.

On 11 October 2004, Guangdong Greencool, Gu Chujun, Greencool procurement center (Shenzhen) Limited (hereafter referred to as Shenzhen Greencool) (格林柯爾採購中心(深圳)有限公司(以下簡稱深圳格林柯爾)) and Agricultural Bank of China Luohu branch (hereafter referred to as Luohu Agricultural Bank) (中國農業銀行深圳羅湖支行(以下簡稱羅湖農行)) signed a Maximum Amount Guarantee Agreement and Supplementary Agreement, which specify that Guangdong Greencool shall provide guarantee for Shenzhen Greencool's debts due to the bank with maximum amount of RMB260,000,000. Within the guarantee period specified by the agreements, Guangdong Greencool promised not to pledge or transfer its holdings of 26.43% shares of the Company to any third party or conduct any other disposal with this holdings; in case the agreements were disobeyed, Shenzhen Greencool shall increase its deposit ratio for unsettled banker's acceptances and unsettled letters of credit to 100%. Based on the above promise, the deposit ratio charged by Luohu Agricultural Bank for banker's acceptances and letters of credit was 20%. The Company did not perform its obligations of reporting and announcement regarding the aforesaid material event and did not disclose it in 2004 annual report.

- (3) The Company did not make a disclosure of the joint investment between Jiangxi Kelon (江西科龍) ("Jiangxi Kelon") and its connected party, Jiangxi Greencool Capital Company Limited (江西格林科爾資本有限公司) ("Jiangxi Greencool") in the 2002 annual report and the 2003 annual report, neither did the Company disclose the use of large amounts of the assets belonging to the connected party in the 2002 annual report and the 2003 Annual report.

In May 2002, Jiangxi Greencool signed an "Entry Agreement into the Development District" with the Management Committee of Nanchang Economic and Technological Development District, pursuant to which the parties agreed to "use their full efforts in supporting the Greencool-Kelon household appliance projects initiated by Greencool Capital Company (格林柯爾資本公司)". In October 2002, Jiangxi Greencool, as the major investor, commenced construction of the production facilities while Jiangxi Kelon, as the other major investor, set up twelve air-conditioner production lines. Such productions lines were put on trial production in November 2003, over 4,000 air-conditioners were produced for that year and 300,000 air-conditioners were produced in 2004. The Company did not disclose the joint investment mentioned above in the 2002 annual Report and the 2003 Annual report, neither did the Company disclose the use of the assets belonging to the connected party in the 2003 annual report and the 2004 annual report.

- (4) The Company did not disclose the joint investment between Zhuhai Kelon Electrical Appliances Company Ltd (珠海科龍電器股份有限公司) ("Zhuhai Kelon") and a connected party, Zhuhai Greencool (Industrial Park) Company Limited (珠海格林柯爾(工業園)有限公司) ("Zhuhai Greencool") in its 2004 annual report.

On 18 May 2003, Shunde Greencool Enterprise Development Company Limited (順德格林柯爾企業發展有限公司) entered into the Greencool Industrial Park Project Agreement (格林柯爾工業園項目協議書) with the People's Government in Jinwan district of Zhuhai city. Pursuant to the Greencool Industrial Park Project Agreement, Zhuhai Greencool was incorporated on 24 September 2003 and Zhuhai Kelon was incorporated in February 2004. Subsequently, Zhuhai Greencool constructed a factory in Qingwan Industrial District in Sanzao town, Jinwan district, Zhuhai city, while Zhuhai Kelon invested in the setting up of the refrigerator production lines and other related equipment within the factory. The Company did not make disclosures of the matters mentioned above in the 2004 annual report.

- (5) The Company did not make a provisional report and announcement on the connected transaction under which the Company purchased from Hefei Meiling Co., Ltd. (合肥美菱股份有限公司) (“Meiling Appliance”) refrigerators and other products in an amount of RMB7,913,900, which was also not disclosed in the Company's 2003 annual report.
- (6) The Company did not make a provisional report and announcement on the connected transaction under which Guangdong Kelon Air-Conditioner Co., Ltd. purchased from Jiangxi Kecheng Industrial Trading Co., Ltd. (江西科盛工貿有限公司) (“Kecheng Industrial Trading”) the Greencool R411C refrigerant, which was also not disclosed in the Company's 2004 annual report.

Further, the Company has committed illegal acts for failing to disclose material connected transactions from 2000 to 2001: (1) the Company did not disclose the cash flows with Guangdong Kelon (Rongsheng) Group Co., Ltd. (廣東科龍(容聲)集團有限公司) (“Rongsheng Group”); (2) the Company did not disclose in accordance with relevant regulations the repayment by Rongsheng Group of the bank loan made on the Company's behalf; (3) the Company did not disclose in accordance with relevant regulations the guarantees provided by it for Rongsheng Group and the performance of such guarantee; (4) the Company did not disclose in accordance with relevant regulations its payment of the amount for delivered goods due to Guangdong Sanyang Kelon Refrigerators Co., Ltd. (廣東三洋科龍冷櫃有限公司) on behalf of Rongsheng Group; (5) the Company did not disclose in accordance with relevant regulations the interests received by it from Rongsheng Group for capital utilisation; (6) the Company did not disclose in accordance with relevant regulations the Promotion Expense Amortisation Agreement (《推廣費用攤銷協議》) entered into between its subsidiary and Rongsheng Group; and (7) the Company did not disclose the transfer of the accounts receivable due from Rongsheng Group to the accounts receivable due from Greencool.

Meanwhile, the CSRC has subjected Gu Chu Jun to the public security authority of the People's Republic of China (the “PRC”) for further investigation in accordance with relevant laws after the CSRC found that Gu Chu Jun was suspected of embezzling and misappropriating huge amounts of the Company's assets.

The above conducts of the Company were in breach of the relevant requirements of Articles 59, 60, 61 and 62 of the Securities Laws of the PRC, which constitute the misconduct as described in Article 177 of the Securities Laws of the PRC as “failing to disclose information in accordance with relevant regulations or disclosing information which contains a falsehood, misleading statement or major omission”.

## II. PENALTY DECISIONS

According to the matters, nature, circumstances and the level of social damage of the offences of the Company and in accordance with Article 177 of the Securities Law of the PRC, the CSRC decided on the following penalties:-

1. A fine of RMB600,000 on the Company;
2. A warning to and a fine of RMB300,000 on Gu Chu Jun;
3. A warning to and a fine of RMB200,000 on Liu Cong Meng, Yan You Song and Zhang Hong, respectively;
4. A warning to and a fine of RMB100,000 on Gary Li Chi Sing, Jiang Bao Jun, Yan Guo Ru, Li Zhen Hua and Fang Zhi Guo, respectively; and
5. A warning to and a fine of RMB50,000 on Chen Pi Chang, Li Kung Man and Xu Xiao Lu, respectively.

*Note:* The meaning of “Connected transaction” and “Connected Party/Parties” as mentioned in this announcement has the same meaning as defined pursuant to the relevant PRC laws and regulations.

### Trading in the H Shares

At the request of the Company, trading in the H Shares of the Company was suspended with effect from 10:00 a.m. on 16 June 2005 pending the release of an announcement in relation to price sensitive information. Subject to the publication of the results announcement of the Company for the financial year ended 31 December 2005 and further announcements in relation to, among others, the financial, production and trading position of the Group, and the satisfaction by the Stock Exchange of Hong Kong Limited to the adequacy of the internal control measures of the Company, trading in the H Shares of the Company will remain suspended until further notice.

By order of the Board of  
**Guangdong Kelon Electrical Holdings Company Limited**  
**Tang Ye Guo**  
*Chairman*

*As at the date of this announcement, the Company’s executive directors are Mr. Tang Ye Guo, Ms. Yu Shu Min, Mr. Su Yu Tao, Mr. Xiao Jian Lin, Mr. Lin Lan and Mr. Zhang Ming; and the independent non-executive directors are Mr. Zhang Sheng Ping, Mr. Lu Qing and Mr. Cheung Yui Kai, Warren.*

Foshan City, Guangdong, the PRC, 4 July 2006

“Please also refer to the published version of this announcement in China Daily”