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粵海制革有限公司

GUANGDONG TANNERY LIMITED

(Incorporated in Hong Kong under the Companies Ordinance, Cap. 32)

INVESTIGATION INTO “ROGUE” OPERATIONS IN THE PEOPLE’S REPUBLIC OF CHINA & RESUMPTION OF TRADING

- Discovery by the GD Tannery Group that certain former executives (“Rogue Executives”) of Nanhai Tannery & Leather Products Co. Ltd. (“Nanhai Tannery”) had been running a “rogue” operation in Nanhai in parallel to the legitimate operations of Nanhai Tannery and on occasions using Nanhai Tannery’s name and resources in doing so, and involving various irregularities in their transactions under the applicable PRC laws and regulations.
- An internal audit team of the Company’s holding companies, working with the new management, conducted a preliminary investigation of the irregularities. The investigation revealed that the Rogue Executives apparently operated a business in parallel to the operations of Nanhai Tannery for their own personal gain.
- The relevant PRC authorities, having been alerted to the rogue operation by the Company, have detained the Rogue Executives involved for investigation. The rogue operation has stopped. The day-to-day operations of the Nanhai Tannery are continuing as normal.
- The Company’s auditors and local PRC lawyers have been instructed to carry out special investigations to ascertain the extent of the rogue operation as well as the extent of any potential liability of the GD Tannery Group.
- It has not been possible for the Company to further their investigations at this stage as a result of the detention of the Rogue Executives involved as well as the PRC authorities’ seizure of all relevant documents for their investigation.
- Based on the findings of the auditors and the advice of the PRC lawyers, the directors of the Company are of their opinion that the rogue operation should not have been incorporated in the financial statements of the Group. However, the rogue operation appears to have breached certain PRC laws and regulations.

- Potential liability of the GD Tannery Group is presently not clear. Contingent liabilities may lie in respect of claims, if any, by the PRC authorities whose investigations are ongoing. It is presently not possible to ascertain with certainty the consequential action that may be taken by the PRC authorities. Since the legal consequences are uncertain, the contingent liabilities are not presently capable of being quantified. As of the date of this announcement, no claim has been made by the PRC authorities.
- Further announcement if necessary to be made in due course.
- Trading in the shares of the Company was suspended at the request of the Company with effect from 9:30 a.m. on 6 August 2002 pending the publication of its announcement regarding the investigations by the Company into the rogue operation and the release of its interim results. Application has been made to The Stock Exchange of Hong Kong Limited for the resumption of trading in the shares of the Company with effect from 9:30 a.m. on 7 August 2002.
- **Investors should exercise caution when dealing in shares in GD Tannery in the meantime.**

Shortly following the change in senior management of the Company in June 2002, it was discovered that certain former executives (“Rogue Executives”) of Nanhai Tannery & Leather Products Co. Ltd. (“Nanhai Tannery”), one of whom, Zhang Muhan, was also a former director of the Company, had been involved in a deception against the Company for illegal personal gain. Nanhai Tannery is a wholly owned subsidiary of the Company and is a sino-foreign cooperative joint venture company established in the People’s Republic of China (“PRC”).

An internal audit team assigned by the holding companies of the Company working together with the new management to investigate the deception discovered in June 2002 that the Rogue Executives had been running a “rogue” operation in Nanhai in parallel to the legitimate operations of Nanhai Tannery and on occasions using Nanhai Tannery’s name and resources in doing so. The rogue operation appeared to have involved various irregularities in their transactions under the applicable PRC laws and regulations.

In late June 2002 the Company reported the rogue operation to the relevant PRC authorities who have detained the Rogue Executives in the Nanhai Municipality for investigations. At about the same time, the Company instructed its auditors and local PRC lawyers to carry out special investigations with a view to ascertaining the extent of the rogue operation as well as the extent of any potential liability of the Group and the Group’s possible recourse against the Rogue Executives. However, it appears at present that the business generated by the rogue operation would not have been available to the Group due to the irregularities in those transactions.

The turnover of the Nanhai Tannery contributed about HK\$137 million (approximately 43.7%) to the GD Tannery Group’s turnover of HK\$314 million for the six months’ period ending 30 June 2002. For the same six months’ period, the GD Tannery Group’s loss of HK\$182 million includes the loss of Nanhai Tannery of HK\$4.5 million (approximately 2.5%).

As at 30 June 2002 the value of the net assets of Nanhai Tannery is approximately HK\$44 million and constitutes 14.23% of the value of the consolidated net assets of the GD Tannery Group of approximately HK\$309 million.

Investors and shareholders should note that the rogue operation has not been incorporated into the interim financial statements of the Group which have also been announced today. Based on the findings of the auditors and the advice of the PRC lawyers, the directors of the Company are of the opinion that it is correct that the rogue operation should not be incorporated in the financial statements of the Group. However, since the rogue operations were elaborate and their transactions were complex, the legal consequence which may arise as a result are uncertain. Therefore, Nanhai Tannery may have contingent liabilities in respect of claims, if any, by the PRC authorities arising out of the various irregularities on the part of the Rogue Executives. Such contingent liabilities are not presently capable of being quantified.

As a result of the detention of the Rogue Executives in the PRC by the PRC law enforcement authorities as well as the authorities' seizure of all relevant documents relating to the rogue operation for their investigations, it has not been possible for the Company and its advisors to further their investigations at this stage.

Investors and shareholders should note that as at the date of this report, there has been no claim against Nanhai Tannery by the PRC authorities. As the investigations of the PRC authorities are still ongoing, it is not possible to ascertain with certainty the consequential actions that may be taken by the PRC authorities in respect of the irregularities and the existence or otherwise of any penalties and claims.

An ad hoc working group comprising the new directors, namely Mr. Xiong Guangyang, Mr. Zeng Haipeng and Mr. Hui Wai Man, has been handling the matter since June 2002.

A board committee to handle the issue was established by the Board on 24 July 2002 which includes one independent director.

As appears from the summarised interim results announcement issued separately by the Company today, the Board has resolved that the Group has made an impairment loss on goodwill arising from the acquisition of Nanhai Tannery. This was identified only about 4 working days before this announcement was provided to the Exchange for approval and on that basis a profits warning preceding this announcement was considered unnecessary by the Board.

If necessary, the Board will make a further announcement as soon as it considers it is able to do so.

Trading in the shares of the Company was suspended at the request of the Company with effect from 9:30 a.m. on 6 August 2002 pending the publication of its announcement regarding the investigations by the Company into the rogue operation and the release of its interim results. Application has been made to The Stock Exchange of Hong Kong Limited for the resumption of trading in the shares of the Company with effect from 9:30 a.m. on 7 August 2002.

In the meantime investors should exercise extreme caution when dealing in shares in GD Tannery.

By Order of the Board
Guangdong Tannery Limited
Xiong Guangyang
Chairman

Hong Kong, 6 August 2002

“Please also refer to the published version of this announcement in The Standard”.