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YUHUA ENERGY HOLDINGS LIMITED

裕華能源控股有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 2728)

CLARIFICATION ANNOUNCEMENT IN RELATION TO THE ANNUAL RESULTS ANNOUNCEMENT OF THE COMPANY FOR THE YEAR ENDED 31 DECEMBER 2018

AND

THIRD SUPPLEMENTAL ANNOUNCEMENT IN RELATION TO THE ANNUAL RESULTS ANNOUNCEMENT AND THE ANNUAL REPORT OF THE COMPANY FOR THE YEAR ENDED 31 DECEMBER 2018

Reference is made to the annual results announcement for the year ended 31 December 2018 (the “**2018 Results Announcement**”) of Yuhua Energy Holdings Limited (the “**Company**”, together with its subsidiaries, the “**Group**”) dated 29 March 2019, the supplemental announcement of the Company dated 11 April 2019 (the “**Supplemental Announcement**”), the 2nd supplemental announcement of the Company dated 23 April 2019 (the “**2nd Supplemental Announcement**”) and the annual report of the Group for the year ended 31 December 2018 (the “**2018 Annual Report**”). Unless otherwise defined, capitalized terms used in this announcement shall have the same meanings as defined in the Annual Results Announcement.

CLARIFICATION

The Company noted that there were inadvertent typographical errors in the 2018 Results Announcement and would like to make the clarification that in the 3rd paragraph on page 30 of the 2018 Results Announcement, the statement should read as “For the two years ended 31 December 2016 and 2017, we generated approximately RMB37.26 million and RMB44.90 million gross profit from fuel oil products business in which approximately 70% and 14% oil products were supplied by Baota”.

AUDIT QUALIFICATIONS

With regards to the section headed “Independent Auditor’s Report — Basis for Disclaimer of Opinion” on the 2018 Annual Report due to the existence of material uncertainties relating to going concern and their possible cumulative effect on the consolidated financial statements, as well as the insufficiency in appropriate audit evidence to them to form a basis for an audit opinion. The Board would like to provide further information in relation to the following audit qualifications:

Management’s view on the Audit Qualification

(1) *Going Concern*

The Company’s consolidated financial statements for the 2018 Financial Statements have been prepared on a going concern basis. There are factors that indicated the existence of material uncertainties which may cast significant doubt about the Group’s ability to continue as a going concern. If the Group is unable to continue to operate as a going concern, adjustments would have to be made to write down the carrying values of the Group’s assets to their recoverable amounts, to provide for any further liabilities which might arise and to reclassify the non-current assets and non-current liabilities as current assets and current liabilities. The actual or potential effects of these adjustments cannot be ascertained currently and therefore, have not been reflected in the 2018 Financial Statements, hence leading to the disclaimed opinion from the Company’s auditors, Cheng & Cheng Limited (the “**Auditors**”), details of which were disclosed in the 2018 Results Announcements. The actual or potential effects of these adjustments depends on the outcome of the Group’s plans and measures to improve its liquidity and financial position, and to remediate delayed repayments to financial institutions which are set out in the 2018 Results Announcements.

There was no different view between the Auditors and the Company’s management. The audit committee has reviewed and agreed with the management’s view.

The Group has undertaken number of measures to improve the Group’s liquidity and financial position, and to remediate delayed repayments to financial institutions which are set out in the 2018 Results Announcement. Accordingly, the Directors consider the Group will be able to continue to operate as a going concern. If the Group’s liquidity and financial position is improved during the next year, it is expected that the audit qualification in respect of going concern may be removed in the financial statements for the year ending 31 December 2019.

Action plan of the Group to address the Audit Qualification

Negotiating with the lenders for the renewal of or extension of repayment of existing borrowings upon maturity

The Group has agreed new repayment schedules or renewed the facility for the majority of its borrowings as at 31 December 2018 with the lenders. The Group will continue negotiate with the other lenders for the settlement or renewal of or extension of repayment of remaining borrowings that were overdue or will soon fall due.

Obtaining additional new source of financing as and when needed

The source of funding of the Group shall include (i) funds to be generated from operations; (ii) recover of prepayments and settlement of trade receivables; (iii) refinancing from banks; and (iv) financial support from Mr. Lin Caihuo (“**Mr. Lin**”).

The Group is currently in discussion with Mr. Lin to obtain shareholder’s loan from him to repay a bank loan outstanding principal amount of approximately HK\$26.9 million.

Implementation of its operation plan to accelerate the Group’s sales

Significant amount of the Group’s working capital is currently locked in the trade and other receivables, hindering the operation of the Group. As the Group gradually recovers such working capital, it will be able to resume sales operation to a normal level. The Group plans to recover and grow the energy trading business by exploring new energy trading products, such as natural gas and pursuing new customers, while controlling the operating costs of the Group. For the oil tanker transportation business, the Group will continue to develop the business by purchasing vessels with a younger age and a higher price-performance ratio at a suitable time. The Group will continuously attribute the resources on expanding the upstream and downstream of the business.

Speeding up the collection of the outstanding sales proceeds

The Group has set up a task force responsible for collecting trade and other receivables. The team will actively and frequently liaise with the debtors to urge for timely settlement of the debts. The Group will also use legal means to chase for settlements where appropriate.

Going forward, the Group will make less prepayments to its suppliers, and instead will use letters of credit or make payments in cash only when delivery is scheduled, in order to reduce its liquidity risk.

Controlling costs and containing capital expenditures

For controlling operating costs, the Group has closed its Hong Kong head office and has cut down headcounts. The Group also plans to repay certain borrowings in order to reduce finance costs.

Maintaining good relationship with the Group’s existing lenders so as to ensure that no action will be taken by those lenders to demand immediate repayment in respect of defaults in the past

The Group will maintain close communication with the lenders and negotiate with lenders for renewal of or extension of existing borrowings well in advance prior to maturity.

Obtaining continuing financial support from Mr. Lin

Mr. Lin has expressed his commitment to continue providing financial support to the Group. The Group is currently in discussion with Mr. Lin to obtain shareholder's loan from him to repay a bank loan outstanding principal amount of approximately HK\$26.9 million.

Breakdown of the Group's outstanding borrowings

The table below sets out the breakdown of the Group's outstanding borrowings as at 31 December 2018:

Nature of borrowing	Outstanding principal as at 31 December 2018	Original due date	Latest due date	Overdue date	Overdue principal amount as at 29 March 2019	Overdue interest as at 31 December 2018	Status as at the date hereof
	HK\$ m				HK\$ m	HK\$ m	
Bank loan	26.9	28/9/18	28/9/18	8/8/18	26.9	0.2	(Note 1)
Notes	98.4	28/4/19	28/4/19	N/A	N/A	9.1	(Note 2)
Bank loan	224.2	11/12/18 to 16/5/19	30/3/20	13/9/18	164.9	2.8	(Note 3)
Bank loan	13.0	19/10/18 to 19/3/19	31/1/19 to 31/12/21	19/10/18	13.0	0.5	(Note 4)
Bank loan	<u>34.0</u>	26/9/19	26/9/19	N/A	<u>N/A</u>	<u>0.1</u>	(Note 5)
Total	<u><u>396.5</u></u>				<u><u>204.8</u></u>	<u><u>12.8</u></u>	

Notes:

1. The Group is currently in discussion with Mr. Lin to obtain shareholder's loan from him to repay such bank loan.
2. The Group is currently in discussion with the note holder to explore various alternatives to repay the notes, including the issue of new Shares to the note holder. It is expected the parties may reach an agreement by August 2019.
3. The bank has agreed to extend the due date to 30 March 2020.
4. The bank and the Group have agreed new repayment schedules.
5. To the best knowledge of the Directors, the bank is willing to renew the facility upon its maturity.

Company's repayment plan of its borrowing

The Company's repayment plan of its borrowings, which will be financed by (i) funds to be generated from operations; (ii) recovery of prepayments and settlement of trade receivables; (iii) refinancing from banks; and (vi) financial support from Mr. Lin.

Company's Current Operation Status on Energy Trading Business

Significant amount of the Group's working capital is currently locked in the trade and other receivables, hindering the operation of the Group. As the Group gradually recovers such working capital, it will be able to resume sales operation to a normal level. Sales during the first quarter of 2019 remained low. During such period, the

Group had been focusing on internal restructuring, including streamlining corporate structure and human resources, pursuing settlement of trade and other receivables and exploring new energy trading products.

(2) Impairments of trade and other receivables

The directors of the Company (the “**Directors**”) were unable to provide to the Auditors with satisfactory information to form a reasonable judgement on the recoverability of the relevant trade and other receivables. The Auditors could not assess whether the amounts of impairment and carrying amounts of trade receivables and prepayments recognised by the Group were fairly stated in the 2018 Financial Statements. Consequently, the Auditors were unable to determine whether any adjustment to these amounts was necessary, and hence the actual or potential impact on the Company’s financial position cannot be ascertained. Details of the disclaimed opinion of the Auditors were disclosed in the 2018 Results Announcement.

When assessing the recoverability of the trade receivables from 深圳市前海懷德石油化工有限公司 (Shenzhen Qianhai Huaide Petrochemical Co. Ltd.*) (“**Qianhai Huaide**”), the Directors have considered that to their best knowledge, Qianhai Huaide was still maintaining normal operation and based on the management’s communication with Qianhai Huaide, it is willing to settle the trade receivables.

When assessing the recoverability of the prepayment to 上海寶塔石化有限公司 (Shanghai Baota Petrochemical Co., Ltd.*) (“**Shanghai Baota**”), the Directors have considered that (i) it is a subsidiary of Baota Petrochemical Group Co. Ltd. (“**Baota Petrochemical Group**”), a large private enterprise which ranked 98th among the top 500 private enterprises and ranked 24th among the top 500 petrochemical companies in the PRC in 2017. As at 31 December 2017, the total assets of Baota Petrochemical Group amounted to approximately RMB63.7 billion and its debt-to-asset ratio was approximately 49.3%; and (ii) based on the best knowledge of the Directors, Baota Petrochemical Group is still maintaining normal business operation as at the date hereof, and that under the administration of the local government and regulatory authority, Baota Petrochemical Group is endeavouring to obtain financing to settle its bills. 張家港保稅區寶塔石化有限公司 (Zhangjiagang Free Trade Zone Baota Petrochemical Co., Ltd.*) (“**Zhangjiagang Baota**”) is a wholly-owned subsidiary of Shanghai Baota. The Group purchased fuel oil from Shanghai Baota and sold petroleum coke to Zhangjiagang Baota.

In view of the above, the Directors considered there is no evidence that the Group would be unable to recover any of the outstanding receivables and that there is equal chance the debts from Qianhai Huaide, Zhangjiagang Baota and Shanghai Baota can or cannot be recovered and therefore, determined that impairment provision should be made for 50% of the trade receivables and repayments from each of the respective entities.

When assessing the recoverability of the trade receivables of 上海兆邦石油化工有限公司 (Shanghai Zhaobang Petrochemical Co. Ltd.*) (“**Shanghai Zhaobang**”), the Directors have considered that Shanghai Zhaobang is a company under the State Council and has issued a letter to the Group committing to repay the debts by 31

December 2019. Accordingly, the Directors are of the view that there is a high chance that the trade receivables from Shanghai Zhaobang will be recovered and therefore, no impairment had been made on such balance.

The audit committee has reviewed and agreed with the management's position in respect of the amounts of impairment provision made.

There was no different view between the Auditors and the Company's management in respect of the impairment provision made. Notwithstanding, the Auditors did not have enough information to assess whether the amounts of impairment and carrying amounts of trade receivables and prepayments recognised by the Group were fairly stated in the 2018 Financial Statements, leading to the disclaimed opinion.

If the trade receivables and prepayments are subsequently recovered or there are sufficient and appropriate audit evidence to support the expected timing and amounts of settlements from the relevant entities to the satisfaction of the Auditors prior to 31 December 2019, the audit qualifications in respect of impairment of trade and other receivables may be removed in the Company's financial statements for the year ending 31 December 2019.

Unable to Conduct Impairment Assessment

The Company was unable to provide the settlement history of the relevant customers and supplier to the Auditor because the relevant customers and supplier did not make any payments during the year ended 31 December 2018, therefore, there was no settlement history available. The Company was unable to conduct a detailed impairment assessment to the satisfaction of the Auditor because the Company cannot reasonably estimate the expected timing and amounts of settlements from the relevant customers and supplier without any settlement history for more than one year. In addition, there was no subsequent settlements or delivery from the relevant customers and supplier up to the date of the auditor's report. The Company did not procure background search on the relevant customers and supplier because, based on its understanding, the background search would not be able to obtain the recent financial information of the relevant customers and supplier for the purpose of the impairment assessment. Alternatively, the Company has provided public information of the relevant customers and supplier to the Auditor, including corporate credit information of each of the relevant customers and supplier posted on the National Enterprise Credit Information Publicity System and background information of Baota Petrochemical Group contained in its website.

Approach and Expected Timeline to Address the Audit Qualification on impairments of trade and other receivables

At the time of auditing the financial statements of the Company for the year ending 31 December 2019, the Company and the Auditor will assess the expected timing and amounts of settlements from the relevant customers and supplier. If the Company is unable to perform a detailed impairment assessment with explanation about the bases for estimating the expected timing and amounts of settlements from the relevant customers or supplier to the satisfaction of the Auditor during the auditing process, the Company will procure an independent valuation on the outstanding balances from the relevant customers or supplier. The Company will make impairment based on such

valuation. The Auditor has agreed to the aforesaid approach to assess the impairments of the relevant outstanding balances in order to remove the audit qualification in the Company's financial statements for the year ending 31 December 2019.

Settlement of outstanding receivables of Qianhai Huaide

The Company had several discussions with Qianhai Huaide during April and May 2019 regarding the settlement of the outstanding trade receivables owed by Qianhai Huaide. In late April 2019, Qianhai Huaide promised to settle all outstanding trade receivables in May 2019. Up to the date hereof, the Company has yet to receive any settlement from Qianhai Huaide. Qianhai Huaide did not indicate a revised expected time of payment. The Company will continue to urge for payments from Qianhai Huaide as soon as possible.

Latest status of the settlements from Qianhai Huaide, Zhangjiagang Baota, Shanghai Baota and Shanghai Zhaobang

Zhangjiagang Baota settled prepayment of approximately RMB300,000 on 14 May 2019. The Company has and will continue to actively and frequently liaise with the debtors to urge for timely settlement of the debts.

Impairment of Zhangjiagang Baota and Shanghai Baota

Reason led to the recognition of the impairment

Since the beginning of 2018, there were material delays in delivery by Shanghai Baota, which failed to comply with the terms of the supplier contracts entered into between Shanghai Baota and the Group. The Group terminated business cooperation with Shanghai Baota since 31 July 2018 and began to pursue return of the prepayments by Shanghai Baota. During July to November 2018, the Group engaged a PRC law firm to issue letters to Shanghai Baota to demand return of the outstanding prepayments every month-end. On 16 November 2018, A listed company under Baota Petrochemical Group announced that its ultimate controlling shareholder was suspected of committing criminal offence. Thereafter, there were news questioning the liquidity of the Baota Petrochemical Group.

Shanghai Baota did not deliver any products to the Group during 2018 and has not returned any prepayments to the Group up to the date hereof. In view that Shanghai Baota has not been delivering products or returning any of the prepayments to the Group for more than one year, it is uncertain as to the timing and the amount of the prepayments made by the Group to Shanghai Baota that can be recovered or Shanghai Baota has the ability to deliver the products, hence the recognition of impairment loss in such regard.

As the trade receivables from Qianhai Huaide had been overdue for more than one year, it is uncertain as to the timing and the amount of such receivables that will be settled, hence the recognition of impairment loss in such regard.

There was only one transaction between the Group and Zhangjiagang Baota since 2017. Considering the liquidity problem of Baota Petrochemical Group as discussed above and that the trade receivables from Zhangjiagang Baota had been overdue for more than one year, it is uncertain as to the timing and the amount of such receivables that will be settled, hence the recognition of impairment loss in such regard.

Auditors' assessment on the impairment

The Auditors assessed the impairment with reference to the information and documents including (i) breakdown of the trade receivables and prepayment; (ii) settlement history of the customers and supplier; (iii) sales/purchase contracts relating to the outstanding amounts; (iv) background search on the customers and supplier; (v) sales invoices/purchase orders relating to the outstanding amounts; (vi) correspondences between the Group and the customers/supplier to chase for the outstanding amounts; and (vii) details of the impairment assessment.

Steps taken by the Company and Directors to assess the Auditors' concern

The Company has provided the Auditors information to assess the impairment including (i) breakdown of the trade receivables and prepayment; (ii) sales/purchase contracts relating to the outstanding amounts; (iii) sales invoices/purchase orders relating to the outstanding amounts; and (iv) letters issued by a law firm, on behalf of the Company, to Shanghai Baota to demand return of the prepayments.

The Company has set up a task force of five members, led by two executive Directors to pursue the settlement of the receivables. The Company targets to recover at least 50% of the outstanding gross amounts or receive at least 50% of the ordered products from Shanghai Baota in 2019. Based on recent discussion between the Company and Shanghai Baota, Shanghai Baota has preliminarily verbally agreed to return the prepayments in monthly instalments starting from May 2019 up to December 2019. Further, based on recent discussion, Qianhai Huaide has verbally committed to settle the trade receivables in full in May 2019.

The Company has assigned specific members of the task force to follow up on each outstanding account. Mr. Lin, the Chairman and controlling shareholder of the Company will also liaise with the relevant debtors personally. The task force will continue to liaise with the relevant debtors on a progressive approach, firstly by phone discussion, failing which then by physical visits and lastly by legal means to protect the Group's rights, where appropriate.

Management's view and the Auditors' view regarding the impairment assessment

There is no different view between the Auditors and the Company's management regarding the impairment assessment.

Non-impairment of Shanghai Zhaobang

Background of Shanghai Zhaobang

Shanghai Zhaobang was established under PRC law on 14 January 2014 with registered capital of RMB100 million and is principally engaged in the trading of petrochemical products.

Based on the information published on the National Enterprise Credit Information Publicity System, Shanghai Zhaobang is wholly-owned by 中信國安化工有限公司 (Citic Guoan Chemical Co. Ltd.*), which in turn is 55%-owned by 中信國安集團有限公司 (Citic Guoan Group Co. Ltd.*). 中信國安集團有限公司 (Citic Guoan Group Co. Ltd.*) is owned as to 20.94% by 中國中信集團有限公司 (China Citic Group Co. Ltd.*), 19.76% by 黑龍江鼎尚投資管理有限公司 (Heilongjiang Dingshang Asset Management Co. Ltd.*), 17.8% by 珠海合盛源投資管理有限公司 (Zhuhai Hechengyuan Asset Management Co. Ltd.*), 15.81% by 瑞煜(上海)股權投資基金合夥企業(有限合夥) (Ruiyu (Shanghai) Stock Investment Fund LP*), 15.81% by 共和控股有限公司 (Gonghe Holdings Co. Ltd.*) and 9.88% by 天津市萬順置業有限公司 (Tianjin Wanshun Property Co. Ltd.*).

中國中信集團有限公司 (China Citic Group Co. Ltd.*) is wholly-owned by the State Council. 黑龍江鼎尚投資管理有限公司 (Heilongjiang Dingshang Asset Management Co. Ltd.*) is owned by 曹立春 (Cao Lichun*) and 范淑春 (Fan Shuchun*). 珠海合盛源投資管理有限公司 (Zhuhai Hechengyuan Asset Management Co. Ltd.*) is owned by 毛德一 (Mo Deyi*), 馬驍 (Ma Xiao*) and 北京寶鼎百川投資合夥企業(有限合夥) (Beijing Baodingbaichuan Investment LP*). 瑞煜(上海)股權投資基金合夥企業(有限合夥) (Ruiyu (Shanghai) Stock Investment Fund LP*) is owned by 中非信銀(上海)股權投資管理有限公司 (China-Africa Citic Bank (Shanghai) Stock Investment Management Co. Ltd.*) and 平安信託有限責任公司 (Pingan Trust Co. Ltd.*). 共和控股有限公司 (Gonghe Holdings Co. Ltd.*) is owned by 關鑫 (Guan Xin*) and 張岩 (Zhang Yan*). 天津市萬順置業有限公司 (Tianjin Wanshun Property Co. Ltd.*) is owned by 白少良 (Bai Shaoliang*) and 劉玉珍 (Liu yuzhen*).

To the best knowledge of the Directors, save for the sale of products to Shanghai Zhaobang by the Group, there was no past and current relationship between Shanghai Zhaobang and its ultimate beneficial owners, and the Group and its connected persons.

The Company has obtained and reviewed public information of Shanghai Zhaobang, including the background and shareholding information of Shanghai Zhaobang. Despite the Company is unable to obtain detailed financial information of Shanghai Zhaobang, it considered that Shanghai Zhaobang had the ability to settle the payments given Shanghai Zhaobang's State-owned background.

The outstanding trade receivables from Shanghai Zhaobang as at 31 December 2018 amounted to approximately HK\$62.5 million, which were due on 21 June 2018.

To the best understanding of the Directors, the reason for the delayed payment from Shanghai Zhaobang was because Shanghai Zhaobang also had delayed payments from its customers, leading to its tight liquidity. The Group only began business relationship

with Shanghai Zhaobang in June 2018. Based on management's recent discussion with Shanghai Zhaobang, it is expected that the outstanding trade receivables from Shanghai Zhaobang will be settled in full by July 2019.

Auditors' assessment on the impairment

The Auditors assessed the impairment with reference to the information and documents including (i) breakdown of the trade receivables and prepayment; (ii) settlement history of the customers and supplier; (iii) sales/purchase contracts relating to the outstanding amounts; (iv) background search on the customers and supplier; (v) sales invoices/purchase orders relating to the outstanding amounts; (vi) correspondences between the Group and the customers/supplier to chase for the outstanding amounts; and (vii) details of the impairment assessment.

Steps taken by the Company and Directors to assess the Auditors' concern

The Company has provided the Auditors information to assess the impairment including (i) breakdown of the trade receivables; (ii) sales contracts relating to the outstanding amounts; (iii) sales invoices relating to the outstanding amounts; and (iv) the letter from Shanghai Zhaobang committing to settle the outstanding amounts in full by 31 December 2019.

The Company will continue to liaise with Shanghai Zhaobang to urge for the settlement of the trade receivables. Based on the management's recent discussion with Shanghai Zhaobang, it is expected that the outstanding amounts will be settled in full by July 2019.

Management's view and the Auditors' view regarding the impairment assessment

There is no different view between the Auditors and the Company's management regarding the impairment assessment.

Prepayments to Shanghai Baota

Company's view on prepayments under Rule 13.13

The Company is of the view that the Group is principally engaged in trading of fuel oil during the three years ended 31 December 2018 and as advised by the Directors, it is a common industry practice to settle the payments for supply of fuel oil by way of prepayments in order to lock in the price of fuel oil. The prepayments to Shanghai Baota were paid pursuant to the terms of the purchase contracts signed, which contained, among others, the agreed products to be supplied, the supply quantity, the selling price and the delivery deadline. Pursuant to the purchase contracts with Shanghai Baota, the Group is required to settle the purchase price in full prior to delivery of products. The Directors confirm that the terms (including the terms of the prepayments) of the purchase contracts entered into with Shanghai Baota for the supply of fuel oil are similar to the terms of the purchase contracts entered into by the Group with other suppliers selling similar products to the Group. Thus, the Board is of the view that the prepayments are trade nature and do not constitute advance to an entity

under Rule 13.13 of the Listing Rules or financial assistance to Shanghai Baota under Chapter 14 of the Listing Rules, and hence are not subject to announcement requirement.

Detailed terms of prepayment

Pursuant to the terms of the purchase contracts entered into by the Group with Shanghai Baota, the purchase consideration was payable in full prior to delivery of the products. The purchase contracts contained the delivery deadline of the products. The purchase contracts did not specify any settlement schedule in case of non-delivery of oil products by Shanghai Baota and interest receivables on the prepayments. The purchase contracts stated that in case of breach of contract, damages may be claimed by the non-defaulting party against the defaulting party by mutual negotiation between the parties or, if failing to reach a mutual agreement, in accordance with the PRC contract law (合同法).

Reasons for the increase of prepayment to Baota

The Company is of the view that the decrease in the transaction amount with Shanghai Baota in the year ended 31 December 2017 as compared to the year ended 31 December 2016 was mainly due to Shanghai Baota increased the selling prices of its products in 2017. Towards the end of 2017, Shanghai Baota offered to provide the Group will favourable prices. Having considered the prices offered by Shanghai Baota were favourable, the Group agreed to place large orders with Shanghai Baota based on the Group's budget and made prepayments according to the terms of the purchase contracts.

Since the beginning of 2018, the supply of fuel oil in the PRC was limited. Therefore, the Group had repeatedly urged Shanghai Baota to deliver the supplies ordered. During the course of communication with Shanghai Baota, Shanghai Baota committed that they will supply new product types to the Group and offer the Group larger discounts, on the basis that the Group will pay further prepayments by bank entrusted payments. The Group had no knowledge of the liquidity problem of Shanghai Baota at the material time and considered that the delay in delivery of products by Shanghai Baota was due to the supply shortage in the market. Having considered that (i) it would be beneficial to the Group to develop new trading products with Shanghai Baota and to obtain more favourable prices, and (ii) the Group was allowed to make the prepayments by bank entrusted payment instead of cash, such that the prepayments would not affect the liquidity of the Group, the Group agreed to make further prepayments to Shanghai Baota during the first half of 2018. The Group also agreed to make further prepayments in 2018 hoping that it would strengthen the relationship with Shanghai Baota, such that Shanghai Baota will supply the products promptly.

Background of Baota Petrochemical Group

Based on the public information and to the best knowledge of the Directors, Shanghai Baota is a subsidiary of Baota Petrochemical Group, which in turn is controlled by Mr. Sun Hengchao (孫珩超先生). Baota Petrochemical Group was founded in 1997 and is a large private leading petrochemical enterprise which operates in the petrochemical industry and has further expanded into the coal-oil chemical and gas chemical industries, engaging in production, research and development. It ranked 98th among the top 500 private enterprises and ranked 24th among the top 500 petrochemical

companies in the PRC in 2017. As at 31 December 2017, the total assets of Baota Petrochemical Group amounted to approximately RMB63.7 billion and its debt-to-asset ratio was approximately 49.3%. Baota Petrochemical Group is the only private petrochemical group that has obtained “five certificates”, namely Crude Oil Import Quotas and Qualifications, the Qualification for Crude Oil Importation and Application, International Crude Oil Trade Qualification, Product Oil Wholesale Qualification and Fuel Oil Import Qualification, which are approved by the National Development and Reform Commission and Ministry of Commerce.

The Group began procuring fuel oil from Shanghai Baota in 2015. Since then, the Group had also been procuring fuel oil from other subsidiaries of Baota Petrochemical Group, including 廣東寶塔石化有限公司 (Guangdong Baota Petrochemical Co. Ltd.*), 新疆寶塔石化有限公司 (Xinjiang Baota Petrochemical Co. Ltd.*) and Zhangjiagang Baota (collectively, the “**Baota Group**”). The Group had also sold petroleum coke to Zhangjiagang Baota. Save for the supply and purchase of products to and from the Group, the Baota Group had no past or current relationship with the Group and its connected persons.

Commercial rationale for the Group for the prepayment

The revenue generated from the fuel oil products business amounted to approximately RMB3,726.4 million and RMB4,489.7 million for the two years ended 31 December 2016 and 2017, respectively; while the revenue attributable to the supplies of the Baota Group amounted to approximately RMB2,515.3 million and RMB607.2 million, respectively. Therefore, the Company is of the view that the amounts of prepayment made to Shanghai Baota were less than the amounts of revenue generated from the oil products supplied by the Baota Group.

The Group agreed to pay a significant amount of prepayment to Shanghai Baota towards the end of 2017 after having considered the following factors:

- (i) the PRC authority would strengthen the monitoring of sales invoice for fuel oil products beginning in 2018, leading to a tightening of the supply of fuel oil products in early 2018. In order to secure enough supplies, the Group decided to make prepayments to Shanghai Baota, being one of its major suppliers to lock in the supplies.
- (ii) The Group ordered in bulk for more favourable price and made prepayments to lock in such price.
- (iii) The then sales target of the Group’s fuel oil trading business for 2018 was RMB10 billion. In order to secure enough supplies to meet such sales target, the Group placed large purchase orders with the Baota Group.

The Company has reviewed the public information of Baota Petrochemical Group as detailed in the abovementioned information. Having considered the scale of operation of Baota Petrochemical Group and that the historical performance of Shanghai Baota since 2015 was satisfactory, the Company considered Shanghai Baota had the ability to timely provide supplies.

Action plan for Impairment of trade and other receivables

Prepayments to Shanghai Baota and trade receivables from Zhangjiagang Baota

On 2 July 2019, a representative of the Group made an on-site visit to the office of Shanghai Baota and noted that the office is no longer in operation. The Group's representative spoke with an officer of Shanghai Baota responsible for registration of and contact with visitors for Shanghai Baota, and was advised that she will escalate the request of payment by the Company to her supervisors but refused to provide their contact information. The officer also advised that Shanghai Baota's business is currently suspended. In view that the responsible officer of Shanghai Baota is no longer contactable, the Company has discussed with the Auditor and have agreed that the Company will write-off the entire outstanding amount of prepayment from Shanghai Baota and trade receivables from Zhangjiagang Baota in its financial statements for the six months ended 30 June 2019. The Company will seek legal advice for taking legal action against the Baota Group as soon as practicable. The Auditor agreed that the above approach will remove the modified qualification on Shanghai Baota's prepayments and Zhangjiagang Baota's trade receivables for the year ending 31 December 2019.

Trade receivables from Qianhai Huaide and Shanghai Zhaobang

The impairment amount will be determined by measuring the expected credit loss in the following manner.

The Group recognises allowance for expected credit loss (“**ECL**”) for trade receivables through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive, discounted at an approximation of the original effective interest rate. For credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective for the timing of the default. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12 months. At each reporting date, the Group assesses whether the credit risk on a trade receivable has increase significantly since initial recognition. Trade receivables that are individually significant will be separately assessed for impairment.

When making the assessment, the Group compares the risk of default occurring on the trade receivable as at the reporting date with the risk of a default occurring on the financial instrument as at the date of initial recognition and considers reasonable and supportable information that is available without undue cost or effort, including historical and forward-looking information. The Group considers a trade receivable is default when contractual payments are 90 days past due. However, in certain cases, the Group may also consider a trade receivable to be default when internal or external information indicates that the Group is unlikely to receive the outstanding contractual amounts in full before considering any credit enhancements held by the Group. A trade receivable is written off when there is no reasonable expectation of recovering the contractual cash flows.

Based on the aforesaid accounting policy, the relevant trade receivables and prepayments are considered in default. As at 31 December 2019, being the next audit reporting date, the Group will estimate the cash flows that it expects to receive from the subject trade receivables by considering historical and forward-looking information, including but not limited to:

- (i) whether there was any settlement of the trade receivables during the year ending 31 December 2019 and their pattern. If there were regular settlements (e.g. monthly settlements), the Company will estimate the cash flows that it expects to receive from the relevant trade receivables based on such settlement pattern. On the other hand, if there was no regular settlement, the Company will consider the cash flow that it expects to receive from such debtor is nil and will write off the then outstanding balance.
- (ii) whether there is any written agreed payment schedule and whether the debtor has made payments according to such schedule. If the debtor has been making payments according to the agreed schedule, the Company will estimate the cash flows that it expects to receive from the relevant trade receivables based on the agreed payment schedule. On the other hand, if there was no written agreed payment schedule or where there was an agreed payment schedule but the debtor did not make regular settlements according to such schedule, the Company will consider the cash flow that it expects to receive from such debtor is nil and will write off the then outstanding balance.
- (iii) whether there is any other information indicating an increase in credit risk of the relevant debtor, such as the debtor being subject to winding up petition, the Group failing to reach the debtor or the debtor indicated to the Group that they will not settle the outstanding amount in part or in full, in which case there is no reasonable expectation of recovering the contractual cash flows, and the Group will write off the relevant outstanding trade receivables.

The Group will estimate the cash flows that it expects to receive based on the settlement pattern and agreed payment schedule of the debtor up to 31 December 2019. If there have not been regular payments from the relevant debtor, the Group will consider the cash flow that it expects to receive from such debtor is nil and will write off the then outstanding balance.

Separately, the Company and the Auditor have discussed with a valuer regarding the feasibility of conducting valuation on the outstanding trade receivables and the appropriate valuation approach. The valuer advised that since the relevant trade receivables are in default and do not follow the normal settlement pattern, it is infeasible to perform valuation on the outstanding trade receivables.

Further, to clarify, despite a majority amount of the prepayments to Shanghai Baota was outstanding for more than one year as at 31 December 2018, the Group was unable to conduct a detailed impairment assessment to ascertain the recoverability of the amount at the time of preparing the financial statements for the year ended 31 December 2018 mainly because the Baota Group did not fail to delivery products to the Group since they commenced business relationship in 2015 up to late-2017 and there was no definite evidence indicating that the Group was unlikely to receive the outstanding prepayments

in full, despite the long delay in delivering the products by the Baota Group. Similarly, there was no history of default from the other relevant debtors and there was no definite evidence indicating that the Group was unlikely to receive the outstanding trade receivables in full. Therefore, the Group was unable to ascertain the amount of the trade receivables and prepayment that can be recovered and the timing.

The Group will commence preparing for and reviewing the impairment assessment of the relevant trade receivables for the year ending 31 December 2019 around November 2019, which it considers is an appropriate time because it is close to the next audit reporting date and the Group expects to have sufficient information to conduct the assessments then. Currently, it has only been around three months since the Group last conducted the impairment assessment for the year ending 31 December 2018. The Group has been and will continue to liaise with the relevant debtors to agree on the payment schedules and to urge for settlement of the trade receivables according to the agreed schedules, however, there is no updates up to the date of this submission. Therefore, the Group currently still has no sufficient information to assess the recoverability of the trade receivables. The Group considers it requires additional time to assess whether the relevant debtors will settle the outstanding amounts owed and the timing of such payments. And in any event, if the Group is still unable to ascertain the recoverability of the trade receivables with reasonable and supportable information (i.e. failing to reach an agreement on the payment schedule and receiving payments according to the agreed schedule) by November 2019 despite the Group's relentless effort, the Group will consider that there is no reasonable expectation of recovering the relevant trade receivables.

The Company will not make a detailed impairment assessment to the satisfaction of the Auditor now because the Auditor will only assess the Group's financial position when they perform the annual audit for the year ending 31 December 2019. Notwithstanding the Auditors has agreed with the Company the aforesaid action plan in order to remove the modified audit qualification on trade receivables for the year ending 31 December 2019.

Set out below is an ageing analysis of the trade receivables and prepayments of the Baota Group and Shanghai Zhaobang as at 31 May 2019:

Debtor name	Outstanding amount (RMB million)	Age
Shanghai Baota	24.0	11 months
	8.0	12 months
	25.0	14 months
	418.9	17 months
	7.9	18 months
Sub-total	483.8	
Zhangjiagang Baota	33.7	11 months
Shanghai Zhaobang	54.7	11 months

The Company's audit committee agreed that the management of the Group has taken all reasonable actions for addressing the audit modification having considered the following factors:

- (a) the management has taken all reasonable actions to urge for settlements of the relevant trade receivables and prepayments, including (i) calling the respective responsible officer of the relevant debtors from time to time to understand their financial and operational condition, to negotiate for a payment schedule and to urge for settlement of the outstanding balance imminently; (ii) made on-site visit to the office of Shanghai Baota on 2 July 2019 and noted that the office is no longer in operation. The Group's representative spoke with an officer of Shanghai Baota responsible for registration of and contact with visitors for Shanghai Baota, and was advised that she will escalate the request of payment by the Company to her supervisors but refused to provide their contact information. The officer also advised that Shanghai Baota's business is currently suspended. In view that the responsible officer of Shanghai Baota is no longer contactable, the Company has discussed with the Auditor and have agreed that the Company will write-off the entire outstanding amount of prepayment from Shanghai Baota and trade receivables from Zhangjiagang Baota in its financial statements for the six months ended 30 June 2019. The Company will seek legal advice for taking legal action against the Baota Group as soon as practicable. The Auditor agreed that the above approach will remove the modified qualification on Shanghai Baota's prepayments and Zhangjiagang Baota's trade receivables for the year ending 31 December 2019; (iii) made on-site visit to the office of Shanghai Zhaobang on 2 July 2019 and conducted face-to-face discussion with a sales manager and a sales personnel of Shanghai Zhaobang and they verbally re-confirmed that Shanghai Zhaobang has agreed to settle the trade receivables owed to the Group of approximately RMB54.7 million, of which RMB20.0 million is expected to be repaid before 31 October 2019 and the remaining amount is expected to be repaid before 31 December 2019; and (iv) engaging PRC law firm to issue letters to Shanghai Baota during July to November 2018 demanding return of the outstanding prepayments. The management of the Group do not consider it to be an appropriate action to file law suits against Shanghai Zhaobang and Qianhai Huaide at this stage because, based on their experience, once legal proceedings are pursued, the debtors will be reluctant to negotiate further with the Company in a friendly manner. Notwithstanding, it is the intension of the Company that, if it is unable to reach a satisfactory payment schedule with the debtors and receive settlements accordingly towards the end of 2019 despite relentless efforts, it will seek legal advice in respect of pursuing legal proceedings against the relevant debtors then;
- (b) the Directors have held various discussions with the Auditor to explore various approaches and action plans to remove the audit qualification in the Company's financial statements for the year ending 31 December 2019; and
- (c) the Company has reached an agreement with the Auditor that the approach set out in action plan above will remove the audit qualification relating to impairment of trade and other receivables in the Company's financial statements for the year ending 31 December 2019.

(3) *Limitation of scope to accounting books and records of the discontinued operations*

The discontinued operations — speaker manufacturing segment (the “**Disposal Group**”) was sold to an independent third party (the “**Purchaser**”) in June 2018 while the Auditors were appointed in February 2019. At the time the Auditors were appointed, the Disposal Group has been taken over by the Purchaser, and the management of the Purchaser refused to provide the books and records prior to the disposal of the Disposal Group for the Auditors’ inspection. Accordingly, the Auditors were unable to access the complete set of accounting books and records of the Disposal Group and to obtain sufficient supporting information to carry out audit procedures to assess whether the relevant financial figures included in the 2018 Financial Statements were fairly stated. Accordingly, the actual or potential impact on the Company’s financial position cannot be ascertained. However, the Directors consider that the uncertainties in respect of such audit qualification will not have a long-term impact on the Group’s financial position.

There was no different view between the Auditors and the Company’s management. The audit committee has reviewed and agreed with the management’s view.

The Auditors were unable to obtain sufficient supporting documentation and explanations to carry out audit procedures relating to (i) the opening balances (as at 1 January 2018) of total assets and liabilities of the Disposal Group of approximately HK\$228.0 million and HK\$186.0 million respectively; (ii) the profit of approximately HK\$1.2 million for the period from 1 January 2018 to 4 June 2018 (effective date of the disposal); and (iii) the deconsolidated assets and liabilities of the Disposed Group as at 4 June 2018 of approximately HK\$176.0 million and HK\$144.0 million respectively. If the books and records of the Disposal Group prior to the disposal was able to be inspected by the Auditors by next year’s audit, the audit qualification may be removed in the Company’s financial statements for the year ending 31 December 2019. Otherwise, audit qualification relating to the 2018 comparative figures will still be issued in the financial statements for the year ending 31 December 2019. However, the audit qualification will be removed in the financial statements for the year ending 31 December 2020 as the figures of the disposal in 2018 will not appear in the financial statements for the year ending 31 December 2020.

Company’s Compliance with Rule 13.09

The Board was of the view that prior to the original due dates of the borrowing, the Group had already initiated negotiation with the relevant financial institutions to renew the borrowings or agree on new repayment schedules. However, during the second half of 2018, the PRC banks had generally tightened up their credit policy and therefore, the negotiation process was prolonged. Given the good relationship between the Group and the relevant financial institutions and the then progress of the negotiations with the financial institutions, the Directors considered the Group would be able reach agreements with them, and hence it was expected that the impact of the delayed repayments would be limited. As at the date hereof, the Group has renewed or extended the repayment of the majority amount of its outstanding borrowings as at 29 March 2019. Accordingly, the Directors did not consider the delayed repayments constituted Inside Information pursuant to Rule 13.09 of the Listing Rules.

Despite there were material delays in delivery by Shanghai Baota and news about the liquidity problem of Baota Petrochemical Group, having considered that, based on the Directors' best knowledge, Baota Petrochemical Group was still maintaining normal business operation, and that under the administration of the local government and regulatory authority, it was endeavouring to obtain financing to settle its bills, the Directors considered there was no evidence that the Group would be unable to recover any of the outstanding prepayments from Shanghai Baota and that there was equal chance the debts can or cannot be recovered. Accordingly, the actual or potential impact on the Group's financial position was still uncertain and hence, the Board was of the view that the information above did not constitute Inside Information pursuant to Rule 13.09 of the Listing Rules.

Directors' fiduciary duties

The Directors were of the view that the prepayments to Baota Group were fair and reasonable and in the interests of the Company and its shareholders as a whole and the decision to make such prepayments were arrived after due and careful consideration, in particular, the Directors have taken into consideration the following factors:

1. the Baota Group was a reputable and established corporation in the petrochemical industry with long history dated back in 1997. It is a leading group with complete supply chain, including oil refining facilities, sales companies and logistic companies. The Baota Group is the only private petrochemical group that has obtained "five certificates", namely Crude Oil Import Quotas and Qualifications, the Qualification for Crude Oil Importation and Application, International Crude Oil Trade Qualification, Product Oil Wholesale Qualification and Fuel Oil Import Qualification, which are approved by the National Development and Reform Commission and Ministry of Commerce.
2. The Group began business relationship with Shanghai Baota since 2015 and had maintained good and stable relationship. There was no default by the Baota Group since 2015 and up to 2017.
3. Up to July 2018 when the Group terminated business relationship with the Baota Group, the Group was not aware of any adverse news about the Baota Group. The Directors would like to emphasize that the majority of the outstanding prepayments to Shanghai Baota was made in November and December 2017, and the Group was not aware of any material delays in delivery by the Baota Group then. The products ordered in November and December 2017 were originally scheduled for delivery in the first half of 2018. Material delays in delivery by the Baota Group only began in the beginning of 2018.
4. The procurement orders placed with the Baota Group during late-November 2017 to June 2018 were determined based on the sales forecasts of the Group for 2018, taking into consideration the framework sales contracts entered into between the Group and its clients. Between 29 November 2017 and 1 December 2018, the Group entered into several framework sales contracts with various clients which targeted a total sales amount of approximately RMB1,200 million of fuel oil for 2018.

5. The Group decided to place significant amount of procurement orders with the Baota Group over other suppliers because the Baota Group offered more favourable prices of approximately 2.2% as compared to the then prevailing market price.
6. For illustrative purpose, based on the sales target for 2018 of approximately RMB1,200 million, the estimated cost of sales would be approximately RMB1,188 million (adopting a gross profit margin of 1% based on the Group's historical financial performance). Accordingly, the prepayment to the Baota Group of approximately RMB483.8 million as at 31 December 2018 was equivalent to approximately 40% of the estimated purchase costs of the Group for 2018. This proportion is consistent with the Group's proportion of purchase from the Baota Group in 2015 and 2016 of approximately 46% and 70%, respectively. The decrease in the transaction amount with the Baota Group in 2017 as compared to 2015 and 2016 was mainly due to the Baota Group increased the selling prices of its products in 2017. Given the Baota Group offered favourable prices in late-2017, it is a preferred supplier of the Group in view of its good business relationship with the Group and its leading position in the petrochemical industry.
7. The Group had no knowledge of the liquidity problem of the Baota Group at the material time and considered that the delay in delivery of products by Shanghai Baota in 2018 was due to the supply shortage in the market. The Group also experienced delayed deliveries by other suppliers at the material time.
8. The procurement with the Baota Group and the prepayments made to the Baota Group were approved according to the procurement policy of the Group, which were approved by each of the procurement manager, finance manager and Mr. Lin, an executive Director, and acknowledged by Mr. Wang Enguang, the then other executive Director.
9. The prepayments to Shanghai Baota were made according to the terms of the purchase contracts, and are in line with industry practice and the terms of similar purchase contracts of other suppliers of the Group. Similarly, the Group also received prepayments from its customers. It is an industry practice to make prepayments to lock in the prices.

In light of the foregoing, the Directors (including the independent non-executive Directors) considered the prepayments to Shanghai Baota were in line with industry practice, fair and reasonable and in the interests of the Company and its shareholders as a whole at the material time.

Accordingly, Mr. Lin, the executive Director on the Board at the material time (the other executive Director on the Board at the material time, Mr. Wang Enguang resigned on 31 May 2019) is of the view that he has fulfilled his fiduciary duties and duties of skill, care and diligence as required under Rule 3.08 of the Listing Rules when approving the prepayments to Shanghai Baota.

Company's compliance of Chapters 13 and 14

Chapter 13 Advance to an Entity

The Company was in the view that the Company was in compliance with the Rules 13.13, 13.14 and 13.20 of the Listing Rules regarding the prepayments made to Shanghai Baota because the prepayments were of trade nature that arose in the Group's ordinary and usual course of business.

Pursuant to Rule 13.15A of the Listing Rules, any trade receivables is not regarded as a relevant advance to an entity if it arose in the issuer's ordinary and usual course of business (other than as a result of the provision of financial assistance); and the transaction from which the trade receivable arose was on normal commercial terms.

Pursuant to the purchase contracts with the Baota Group, the Group is required to settle the purchase price in full prior to delivery of products. The outstanding prepayments to Shanghai Baota as at 31 December 2018 were all made pursuant to corresponding purchase contracts. The Director confirm that the terms (including the terms of the prepayments) of the purchase contracts entered into with the Baota Group for the supply of fuel oil are similar to the terms of the purchase contracts entered into by the Group with other suppliers selling similar products to the Group, and are on normal commercial terms, fair and reasonable.

Further, as confirmed by the Auditor, the prepayments to Shanghai Baota were classified as trade nature in the financial statements of the Company.

Accordingly, the Directors do not consider the prepayments to Shanghai Baota were subject to disclosure requirements pursuant to Rules 13.13, 13.14 and 13.20 of the Listing Rules.

Chapter 14 Notifiable Transactions

The prepayments made to Shanghai Baota were of trade nature that arose in the Group's ordinary and usual course of business. The outstanding prepayments to Shanghai Baota as at 31 December 2018 were all made pursuant to corresponding purchase contracts. The Directors consider the prepayments made to Shanghai Baota were commercial justifiable, on commercial terms, fair and reasonable. The Directors were of the view that the fact there had been delays in delivery of products by the Baota Group did not imply the prepayments were of financing nature. Further, as confirmed by the Auditor, the prepayments to Shanghai Baota were classified as trade nature in the financial statements of the Company.

Accordingly, the Directors did not consider the prepayments constitute financial assistance pursuant to Rule 14.04(1)(e) of the Listing Rules and the Company was not in breach of the reporting, announcement and shareholders' approval requirements under Rules 14.34 and 14.40 of the Listing Rules regarding each of the Previous Prepayments and the Further Prepayments.

The Board confirms that the above supplemental information does not affect other information contained in the Annual Results Announcement, the Supplemental Announcement and the 2nd Supplemental Announcement and the content of the Annual Results Announcement, the Supplemental Announcement and the 2nd Supplemental Announcement remains correct and unchanged.

By Order of the Board
Yuhua Energy Holdings Limited
Yuan Hongbing
Executive Director

Hong Kong, 19 July 2019

As at the date of this announcement, the Company has three executive Directors, namely Mr. Lin Caihuo (Chairman), Mr. Chen Jinle and Mr. Yuan Hongbing, one non-executive Director, namely Mr. Wang Shoulei, and three independent non-executive Directors, namely Mr. Tche Heng Hou Kevin, Mr. Liu Yang and Mr. Xu Changyin.

** for identification purposes only*