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**Hilong Holding Limited**

**海隆控股有限公司\***

*(Incorporated in the Cayman Islands with limited liability)*

**(Stock Code: 1623)**

**INSIDE INFORMATION  
KEY FINDINGS OF THE INDEPENDENT INVESTIGATION  
AND  
CONTINUED SUSPENSION OF TRADING**

This announcement is made by Hilong Holding Limited (the “**Company**”, together with its subsidiaries, the “**Group**”) pursuant to Rule 13.09(2) of the Rules Governing the Listing of Securities (the “**Listing Rules**”) on The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) and the Inside Information Provisions under Part XIVA of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong).

References are made to the announcements of the Company dated 19 March 2024, 25 March 2024, 30 April 2024, 31 May 2024, 18 June 2024, 28 June 2024, 8 July 2024, 22 August 2024 and 27 September 2024 in relation to, among others, the delay in publication of the 2023 Annual Results announcement and despatch of the 2023 Annual Report, the postponement of the Board meeting and the 2024 annual general meeting, the establishment of the Investigation Committee, the resignation of PricewaterhouseCoopers as the auditor of the Company, the Resumption Guidance, the quarterly update on status of Resumption in June 2024, the appointment of Crowe as the new auditor of the Company, further delay in publication of the 2023 Annual Results and despatch of the 2023 Annual Report and delay in publication of the 2024 Interim Results and despatch of the 2024 Interim Report, and the quarterly update on status of Resumption in September 2024 (collectively, the “**Announcements**”). Unless otherwise indicated, capitalised terms used herein shall have the same meanings as defined in the Announcements.

**BACKGROUND**

As disclosed in the Announcements, during the course of the audit process for the year ended 31 December 2023, PricewaterhouseCoopers (the “**Former Auditor**”), the former auditor of the Company, set out certain key unresolved audit issues (the “**Key Audit Issues**”) and other matters that shall be brought to the attention of the shareholders (“**Shareholders**”) and the creditors (“**Creditors**”) of the Company. The key audit issues include, among others, the sale and procurement of pipe materials involving four Russian subsidiaries of the Group (“**Russian Subsidiaries**”) and a company established in Russia (“**Entity A**”) from 1 October 2022 to 31 December 2023 (the “**Transactions**”).

At the Former Auditor's request, the Investigation Committee engaged Ernst & Young (China) Advisory Limited (the "**Independent Advisor**") on 12 March 2024, an independent third party based on the best knowledge, information, and belief of the Directors, as the forensic accounting specialist to conduct an independent investigation into the Transactions and related business dealings of Entity A (the "**Investigation**").

In line with the requirements set out in the Resumption Guidance in the Company's announcement dated 18 June 2024 and, in any event, in order properly to address the issues arising in the best interests of Shareholders and potential investors, the Company has conducted an appropriate independent investigation into the matters relating to the Transactions, assess their impact on the Company's business operation and financial position, announce the findings and take appropriate remedial actions. The Independent Advisor issued the report of the Investigation dated 30 September 2024 (the "**Investigation Report**").

## **SCOPE OF INVESTIGATION**

The Independent Advisor conducted forensic investigation into the Transactions and related business dealings of Entity A involving four Russian Subsidiaries of the Group, namely Drilling Technology Limited Liability Company ("**Drilling Technology**"), Technomash LLC ("**Technomash**"), Hilong Petroleum Pipeline Service (Surgut) LLC ("**Pipeline Surgut**") and Hilong Petroleum Pipeline Service (Orenburg) Limited Liability Company ("**Pipeline Orenburg**"), which took place during the period from 1 October 2022 to 31 December 2023 (the "**Review Period**").

The scope of the Investigation covered the following aspects: (i) background information of Entity A and its relationship with the Company and the Russian Subsidiaries, (ii) the details and commercial rationale of the Transactions; (iii) the credit facilities and financings obtained by Entity A; (iv) the payment of marketing expenses by the Russian Subsidiaries through Entity A; and (v) the Board's and the senior management's knowledge of and involvement in the Transactions and other related business dealings of Entity A, and whether those transactions were properly approved, subject to the limitations as set out in the section headed "Limitations" below.

## **MAJOR PROCEDURES OF INVESTIGATION**

For the purpose of the Investigation, the Independent Advisor conducted the following review procedures, including but not limited to:

1. performing background checks on Entity A and its related personnel through public channels;
2. obtaining and reviewing relevant documents including Board minutes, the Company's relevant policies, approval procedures, financial records, the Russian Subsidiaries' bank transaction records, guarantee contracts, assessment of the financial impact of the Transactions and other relevant supporting documents;
3. reviewing and analysing procurement and sales orders of the Transactions during the Review Period and obtaining samples for review;

4. reviewing Entity A's shareholder agreements, registration documentation, board minutes, articles of association, sales and purchase ledgers, reconciliation records with suppliers, bank ledgers, cashflow management reports, e-banking statements, bank loan agreements and other banking documents, and employment contracts;
5. analysing Entity A's financial records and bank statements, and performing reconciliation on the sales and procurement transactions and fund flows between the Russian Subsidiaries and Entity A; the usage of bank loan proceeds by Entity A; procurement by Entity A from certain suppliers; and the flow of Entity A's dividend funds;
6. conducting interviews with members of the Board, certain senior management of the Company and relevant personnel of the Group to understand the facts and circumstances leading up to the establishment of Entity A and its subsequent dealings with the Russian Subsidiaries;
7. conducting interviews with Entity A's PRC suppliers to understand their transactions with Entity A and their relationship with the Russian Subsidiaries;
8. obtaining confirmations from depositary bank of Entity A and major suppliers in relation to their transactions with Entity A and balances as of 31 December 2022 and 2023; and
9. conducting computer forensics procedures to retrieve and review electronic data from the devices and/or email servers of the executive Directors of the Company, certain senior management of the Company and relevant personnel of the Group.

## **SUMMARY OF KEY FINDINGS AND OBSERVATIONS FROM THE INVESTIGATION**

### **1. Background and business purposes of the establishment of Entity A**

#### *Background*

- (i) In 2022, the Russian Subsidiaries faced liquidity issues due to a combination of factors, among others, including the following:
  - a. The Russian Subsidiaries are primarily engaged in oilfield equipment manufacturing and services, and procure pipe materials primarily from a Belarusian supplier ("**Supplier B**"). The Company advised that while Supplier B requires upfront prepayments for the procurement of pipe materials, generally the corresponding sales collection of the Russian Subsidiaries from third parties could not keep up with Supplier B's demands for prepayments.
  - b. In light of the depreciation of Rubles against RMB in 2022 because of geopolitical factors, the Russian business division of the Group decided to exchange a substantial amount of Rubles to RMB to mitigate foreign exchange risk, leaving minimal amount of Rubles for local daily operations.

- c. Following the designation of the Russian bank (“**Bank C**”) that provided loan financing to the Russian Subsidiaries in the past on the OFAC’s Specially Designated Nationals and Blocked Persons (“**SDN**”) List in 2022, the Group requested the Russian Subsidiaries to avoid dealing with Bank C.
- (ii) From May to November 2022, the Russian Subsidiaries attempted to seek alternative financing channels from a local bank in Russia that was not on the SDN List, however, the Russian Subsidiaries were unable to agree terms with the bank and hence did not proceed with the loan application.
- (iii) Followed the above, a finance employee of Drilling Technology (“**Employee A**”) proposed setting up an intermediary supplier to obtain loan financing from Bank C, and in turn funding the required prepayments to Supplier B and other operating activities of the Russian Subsidiaries. The proposed arrangement was reported to and agreed by the general manager of Drilling Technology and Technomash, the finance director of the Russian region and the general manager of the Russian region (together, the managers of the Russian Subsidiaries (“**Russian Managers**”)), and verbally approved by the general manager of the oilfield equipment manufacturing and services segment of the Group (“**General Manager of the Oilfield Equipment Segment**”) who confirmed that he did not further report to or seek approval from his managers at the Group level in relation to the establishment of Entity A, including the Company’s executive president (“**Executive President**”), chief financial officer (“**CFO**”) and executive Directors.
- (iv) Entity A was established on 23 September 2022 and became an intermediary supplier of the Russian Subsidiaries in October 2022. Employee A is Entity A’s sole shareholder, general manager and the sole authorised signatory for its transactions with local banks.

*Business purpose*

- (v) In light of the background set out above, and based on the Independent Advisor’s review of internal email communications of the relevant personnel of the Russian Subsidiaries, and clarifications sought during interviews, it is understood that the business purposes of the establishment of Entity A are as follows:
  - a. to assist the Russian Subsidiaries with alternate means of financing; and
  - b. to facilitate procurement of pipe materials from Supplier B through prepayments with funds obtained through financing, and in turn selling those pipe materials to the Russian Subsidiaries with a more favourable settlement term (i.e. 180 days after receipt of goods).
- (vi) In order to maintain the above purposes, Entity A earned profits from its trading with the Russian Subsidiaries in order to fund its financing interest expenses as well as certain marketing expenses paid on behalf of the Russian Subsidiaries.

- (vii) As explained by the Russian Managers, since the Russian Subsidiaries did not intend to acquire Entity A and/or consolidate Entity A's financial results into the Group's consolidated financial statements, the Russian Managers and the General Manager of the Oilfield Equipment Segment did not report and seek approval from the Board and/or the senior management of the Company with respect to Entity A's establishment and its subsequent dealings with the Russian Subsidiaries.
- (viii) The Independent Advisor has noted the reporting line within the Group and reviewed different sources of corroborating information collated during the Investigation, including but not limited to the Group's internal approval records; contemporaneous management reporting materials; transactional supporting documentation; internal email communications and electronic documents extracted from computer forensics procedures; and information and representations obtained from interviews. The investigative findings noted the involvement of relevant personnel of both the Russian Subsidiaries and certain senior management members of the Group. The extent of this involvement, including its limits, is summarised in the section below in this announcement headed "4. Involvement of relevant personnel of the Russian Subsidiaries and certain senior management members of the Group regarding the establishment of Entity A and the Bank C Loans" of this announcement. Otherwise, based on the information made available to the Independent Advisor, they have not identified documentary evidence suggesting that the Company's Directors had any decision making role in connection with (a) the establishment of Entity A; (b) the Transactions; and (c) the provision of the Russian Guarantees (as defined below in the section headed "3. Entity A's source of funding").

## **2. Lack of independence of Entity A**

According to the findings of the Investigation, the Independent Advisor had not observed sufficient evidence suggesting that Entity A was operating independently from the Russian Subsidiaries. In fact, there were overlaps in the personnel, day-to-day operations and management reporting process between Entity A and the Russian Subsidiaries, which are summarised as follows:

- (i) Entity A's establishment and important business decisions such as financing plans were determined by the Russian Managers;
- (ii) nine employees of the Russian Subsidiaries and a family relative of Employee A were working part-time at Entity A;
- (iii) Entity A does not have its own sales team or back office. It rented an office from Drilling Technology and has the same registered office address;
- (iv) Employee A is responsible for managing Entity A's finance activities and the general manager of Drilling Technology and Technomash has been delegated by the Russian Managers to oversee Entity A's operation on-site;
- (v) Employee A is the sole authorized signatory for Entity A's bank transactions;

- (vi) Entity A's main source of revenue (FY2022: 99.9%; FY2023: 98.5%) and profit were derived from trading activities with the Russian Subsidiaries; and
- (vii) Entity A's financial data was included in the internal management report of the Russian Subsidiaries in 2023.

### 3. Entity A's source of funding

According to the findings of the Investigation, Entity A's source of funding mainly originated from (i) bank borrowings pursuant to a number of loan agreements entered into with Bank C ("**Bank C Loans**"), which were used to provide liquidity for the Russian Subsidiaries and make prepayments for the procurement of pipe materials; and (ii) trading profits obtained by acting as the Russian Subsidiaries' intermediary supplier.

During the Review Period, Entity A obtained credit line in the aggregate amount of RUB4,250 million from Bank C. The Russian Subsidiaries and Trade House Hilong-Rus Co., Ltd., a wholly-owned subsidiary of the Group based in Russia, together provided guarantees in favour of Entity A to secure the Bank C Loans (the "**Russian Guarantees**"). The primary purpose of the Bank C Loans was to pay for the procurement of pipe and other raw materials from two local suppliers (including Supplier B) and two PRC suppliers by Entity A. The outstanding balance of the Bank C Loans was RUB1,900 million as of 31 December 2022 and RUB1,420 million as of 31 December 2023, respectively.

Prior to obtaining the Bank C Loans, Entity A was required to provide Bank C with a loan utilization plan and relevant supporting documents, such as procurement contracts and orders, to Bank C for review. Upon Bank C's approval, the loan funds were deposited to Entity A's bank account and in turn remitted directly to the relevant suppliers by Bank C. As such, the loan funds were utilised in accordance with the loan agreements.

Since Entity A was required to satisfy Bank C's requirement for borrowers to maintain a profit margin of not less than 8%, the pipe materials procured from Supplier B by Entity A were sold on to the Russian Subsidiaries at a gross profit margin from 8% to 10%.

According to the Investigation Report, the Independent Advisor analysed Entity A's accounting subledgers and bank statements, which were consistent with the Transactions, transactions with its third-party suppliers mentioned above, and the drawdown, usage and repayment of bank loans. They also obtained and analysed the replied confirmations from suppliers that the procurement transaction details and current balance are consistent with the books and records of Entity A; and the replied bank confirmations that the loan balances are also consistent with the books and records of Entity A.

As of 31 December 2023, the total drawdown amount of the Bank C Loans was approximately RUB4,042.7 million. As of the date of this announcement, the outstanding balance of the Bank C Loans is approximately RUB1,340 million.



#### 4. Involvement of relevant personnel of the Russian Subsidiaries and certain senior management members of the Group regarding the establishment of Entity A and the Bank C Loans

The table below sets out the investigation results in relation to the level of involvement of the relevant personnel of the Russian Subsidiaries and certain senior management of the Group:

Entity	Personnel and Position	Summary of Investigation Findings	Level of involvement
Russian Subsidiaries	Employee A	<ul style="list-style-type: none"> <li>Collated documents relating to the Russian Guarantees</li> <li>Received Entity A fund flow schedules on routine basis</li> <li>Responsible for reviewing and approving each fund flow transaction of Entity A, and directly liaised with banks regarding financing matters</li> </ul>	Daily operations and execution of Entity A's activities
	General manager of Drilling Technology and Technomash	<ul style="list-style-type: none"> <li>Aware of the establishment of Entity A and the Bank C Loans; and signed-off weekly payment plan of Entity A</li> <li>Responsible for supervising and reviewing Entity A's operations per instructions of the finance director and general manager of the Russian region</li> </ul>	On-site supervision and review of Entity A's daily operations
	Then finance director of the Russian region (currently the finance director of the Oilfield Equipment Segment)	<ul style="list-style-type: none"> <li>Aware of the establishment of Entity A, the Bank C Loans and the Russian Guarantees</li> <li>Reporting the establishment of Entity A and its business purpose to seek alternative financing; reporting the usage of the Bank C Loans to the oilfield equipment manufacturing and services segment ("<b>Oilfield Equipment Segment</b>"); Coordinating financing plans in Russia, including planning the usage of the Bank C Loans</li> </ul>	Instructing the general manager of Drilling Technology and Technomash to supervise and review the operations of Entity A, and planning of Entity A's financing
	General manager of the Russian region	<ul style="list-style-type: none"> <li>Aware of the establishment of Entity A and the Bank C Loans; received reports of the establishment of Entity A to seek alternative financing; and signed certain Russian Guarantees documents</li> <li>Verbal discussion with the general manager of Drilling Technology and Technomash, and the finance director of the Russian region in relation to the establishment of Entity A and the Russian Guarantees, and verbally report and seek approval from the General Manager of the Oilfield Equipment Segment regarding the aforementioned matters</li> </ul>	Instructing the general manager of Drilling Technology and Technomash to supervise and review the operations of Entity A

Entity	Personnel and Position	Summary of Investigation Findings	Level of involvement
Oilfield Equipment Segment	Vice manager of the Oilfield Equipment Segment	<ul style="list-style-type: none"> <li>Aware of the establishment of Entity A and the Bank C Loans; received reports regarding the Russian Guarantees; reviewed the segment's reporting materials for the 1st quarter of 2023 and agreed with the request from the finance director of the Russian region to remove information of the Bank C Loans in the said report for further upward reporting to the CFO; and received reports relating to the usage of the Bank C Loans</li> <li>Oversight of businesses of oilfield equipment manufacturing and services</li> </ul>	Received and reviewed business reports of the Oilfield Equipment Segment, including the Bank C Loans and the Russian Guarantees
	Mr. Cao Yuhong ("Mr. Cao") (General Manager of the Oilfield Equipment Segment)	<ul style="list-style-type: none"> <li>Verbally approved the proposed establishment of Entity A</li> <li>Recipient of emails relating to the progress of the Russian Guarantees and the usage and application of the Bank C Loans</li> </ul>	Provided verbal approval
Group level	Internal audit officer of the Group	<ul style="list-style-type: none"> <li>Prepared risk management report to be presented to the Board, which included narrative of financing obtained in the Russian region in the amount of RUB1,900 million (incidentally resemble the amount of the Bank C Loans, referred to as Russian financing matter thereunder)</li> <li>Removed the Russian financing matter from the final version risk management report before submitting to the Board</li> </ul>	Had knowledge of the Russian financing that was inconsistent with the disclosure in the Company's 2022 draft annual report, but did not follow up on related matters
	Mr. Chen Yong (CFO)	<ul style="list-style-type: none"> <li>Received email enclosing management report prepared by the Oilfield Equipment Segment, of which the main body and attachment did not contain any information of the Russian financing matters</li> <li>Was not aware of the email chain of said email which revealed prior discussion sent from the finance director of the Russian region seeking agreement from the vice manager of the Oilfield Equipment Segment to remove the Russian financing matters from the management report</li> </ul>	Overlooked internal discussion amongst the management of the Oilfield Equipment Segment regarding the Russian financing matters



Entity	Personnel and Position	Summary of Investigation Findings	Level of involvement
	Mr. Dai Daliang ("Mr. Dai")  (Executive president)	<ul style="list-style-type: none"> <li>Reviewed the draft version of the risk management report prepared by the internal audit officer, which included information of the Russian financing matters. Amongst Mr. Dai's comments in the draft risk management report, he did not provide any comment or edit on the section regarding the Russian financing matter</li> <li>Was not aware that there were inconsistencies between the loan balance in the Russia region and the disclosure in the Company's 2022 draft annual report</li> </ul>	The draft risk management report received and reviewed by Mr. Dai showed indications that there was financing in Russia, and according to Mr. Dai's scope of responsibilities, he should have but did not follow up on the inconsistencies disclosed in the Company's 2022 draft annual report
	Mr. Wang Tao (汪濤)  (Executive director and chief executive officer of the Company)	<ul style="list-style-type: none"> <li>Copied in the email sent by the internal audit officer enclosing the draft risk management report, which included information of the Russian financing matter</li> <li>Since Mr. Dai had replied in the email to the internal audit officer regarding the draft risk management report, Mr. Wang believed that it had been handled and did not further review the draft risk management report</li> </ul>	The draft risk management report received by Mr. Wang showed indications that there was financing in Russia, and according to Mr. Wang's scope of responsibilities, he should have but did not follow up on the inconsistencies disclosed in the Company's 2022 draft annual report

## 5. Transactions between Entity A and the Russian Subsidiaries

### *Repurchase transactions between the Russian Subsidiaries and Entity A*

During the Review Period, the Russian Subsidiaries had entered into six groups of repurchase transactions with Entity A; of which (i) Drilling Technology sold and subsequently repurchased pipe materials from Entity A in five separate groups of transactions; and (ii) Technomash sold and Drilling Technology subsequently repurchased fixed assets and accessories from Entity A (collectively, the “**Repurchase Transactions**”). In respect of the Repurchase Transactions, the total sales amount made by the Russian Subsidiaries to Entity A was RUB1,571 million and the repurchase amount from Entity A by the Russian Subsidiaries was RUB1,728 million, through which Entity A made a gross profit of RUB157 million. For each of the Repurchase Transactions, the repurchase price represented approximately 10% increase of the sales price and therefore the total gross margin on the Repurchase Transactions made by Entity A was approximately 10%.

Based on information gathered from the Russian Managers, the aforesaid Repurchase Transactions were to help Entity A to satisfy Bank C’s profit requirement in order for Bank C to grant the Bank C Loans to Entity A.

In addition, the Independent Advisor noted the following observations as to the potential implications of the Transactions, which included the Repurchase Transactions, on the financial statements of the Russian Subsidiaries:

- (i) due to the lack of commercial substance of the Repurchase Transactions, the revenue and profit recorded in the financial statements of Russian Subsidiaries for FY2022 and FY2023 through Entity A would unlikely count towards the revenue of the Russian Subsidiaries for the relevant periods, and the carrying amount of the corresponding pipe materials and fixed assets and accessories were also likely inflated.
- (ii) other than the Repurchase Transactions, the unit price of pipe materials purchased through Entity A from Supplier B was generally about 8% to 10% higher than that of direct purchases from Supplier B, resulting in the book value of the inventory of pipe materials inflated. When the relevant pipe materials were used in production by the Russian Subsidiaries, the corresponding recognition of production costs were also likely inflated.

As of 31 December 2023, the net outstanding amount due to Drilling Technology and Technomash from Entity A was approximately RUB941.5 million and RUB100.9 million, respectively. An extension agreement for the outstanding payment was signed by the general manager of Drilling Technology and Technomash. On 29 March 2024, Entity A repaid all the outstanding amount to Drilling Technology.

As of the date of this announcement, there was no outstanding amount due to Drilling Technology from Entity A.

The Company sought legal advice from TAXES and FINANCIAL LAW (“**Nalogi i Finansovoe Pravo Agency**”), an independent legal advisor in Russia (“**Russian Legal Advisor**”). The Russian Legal Advisor opined that the Repurchase Transactions between the Russian Subsidiaries and Entity A do not constitute a violation of Russian civil law and no tax exposure risks are found for the parties in such Repurchase Transactions. Further, the Russian Legal Advisor believed that circumstances allow to justify the business purpose of the Repurchase Transactions to relevant tax authorities and noted that the Repurchase Transactions were also included in the materials provided to and accepted by Bank C.

According to the Investigation Report, the Independent Advisor noted that Entity A itself does not possess any commercial relationship allowing it to obtain more favorable credit period or payment terms from suppliers. The Russian Subsidiaries only benefited from Entity A making advance payments for the procurement of raw materials through its bank loans.

## **6. Payment of marketing expenses through Entity A**

According to the Russian Managers, most of the salespersons in Russia were Chinese and faced difficulties in market development and maintaining client relationships in the region. Costs incurred for market expansion activities were recorded as salespersons’ commissions and bonuses in the accounting records of the Russian Subsidiaries. After the establishment of Entity A, a portion of the profits obtained through Entity A as an intermediary supplier was drawn from the bank account of Entity A as dividend payments to Employee A for the purpose of settling Russian Subsidiaries’ marketing expenses. During the Review Period, RUB93.5 million was declared and distributed to Employee A’s personal bank account for onward transmission to relevant salespersons. According to the Investigation Report, although there were internal management notice showing that the overall marketing expense budget was approved by the General Manager of the Oilfield Equipment Segment, the Russian Subsidiaries did not formulate internal policies to approve the individual payment of marketing expenses through Entity A during the Review Period, and the Independent Advisor found no supporting documents nor any management approval to demonstrate the commercial substance of the marketing expenses paid through the dividend payment of Entity A. According to the Investigation Report, the Independent Advisor also noted that the payment of marketing expenses through Entity A as dividend was not authorized by the Board.

According to the Investigation Report, the Independent Advisor noted that, a cooperation agreement was entered into between Drilling Technology and Employee A on 1 August 2024 (the “**Cooperation Agreement**”). Pursuant to the Cooperation Agreement, Employee A would manage Entity A in accordance with Drilling Technology’s instructions, including any amendment to its constitutional documents, restructuring and winding up of Entity A, appointment or removal of management of Entity A, increase or reduction of the share capital of Entity A, and approval of material transactions or related party transactions. Employee A also undertook to replenish Entity A in full any dividend declared to its shareholder. Further, Drilling Technology may purchase Entity

A at the price of RUB10,000 at any time. The Russian Legal Advisor opined that the terms of the Cooperation Agreement do not violate applicable Russian laws, and Drilling Technology may choose to consolidate Entity A's financial position and results into the Group's consolidated financial statements.

As of the date of this announcement, the full amount of RUB93.5 million was recovered from Employee A.

## **7. Lack of approval process involved and compliance with company policies**

According to the findings of the Investigation,

- (i) The Independent Advisor noted that (i) there were no written or internal documents which recorded the business purposes and approval process of the establishment of Entity A; and (ii) the Russian Subsidiaries did not make capital contributions to Entity A. According to the Group's legal management system, material business, financing and guarantee contracts shall be approved by the Group, and the relevant unit shall report to the Group level. It was noted that the establishment of Entity A did not comply with the Group's and the Russian Subsidiaries' internal policies and procedures and was not properly authorized.
- (ii) According to the Group's audit monitoring policy, there shall be no economic dealings between any members of the Group and companies such that an employee or his/her affiliate(s) is interested therein. In any exceptional cases, an employee should fill in a declaration of interest form and obtain prior approval from the management and the Board. Although the employee handbook of the Russian Subsidiaries did not specifically include such conflict-of-interest provision, such prohibition and requirement should have uniformly applied to all departments and members of the Group. The Independent Advisor noted that the establishment of Entity A and the Transactions fall within the definition of conflicts of interest under the Group's policy, but such interest was not declared and no approval from the Group's internal audit department, chief executive officer, Chairman and/or the Board was obtained, which did not comply with the Group's audit monitoring policy.
- (iii) According to Drilling Technology's procurement policy, its procurement department should perform sufficient and appropriate due diligence procedures on the supplier's (including intermediary) capabilities, background, financial data, licenses as part of the onboarding process for suppliers. Although verbal approval was obtained from the General Manager of the Oilfield Equipment Segment, the Independent Advisor noted that the Russian Subsidiaries did not conduct adequate due diligence investigation on and assess the potential transaction risks associated with the onboarding of Entity A, which did not comply with Drilling Technology's procurement policy.

- (iv) According to the Group's financial management policy, the Company in principle shall not provide any guarantees to entities that are not its subsidiaries. Any guarantees provided by the Company to its subsidiaries must be reported to and approved by the Board. If any subsidiary needs to provide external guarantee to a third party due to business development, it must declare the guarantee period, amount, guaranteed party and other necessary details to the Company's Board for approval. The Independent Advisor noted that the Russian Guarantees were verbally discussed among the Russian Managers and reported to the General Manager of the Oilfield Equipment Segment, however, no reporting was made to, and no approvals were obtained from the Board, which did not comply with the Group's financial management policy.

## **8. Financial impact of Entity A on the Group's financial statements**

Based on the Investigation Report, the Independent Advisor noted that the Board was evaluating the financial impact of consolidating Entity A into the Group's financial statements, after consultation with Crowe. After the consolidation, the sales revenue, trade receivables and trade payables between the Russian Subsidiaries and Entity A would be eliminated. The Independent Advisor noted that the Group is anticipated to be exposed to the following impact, among other things, on its financial position as of 31 December 2022 and results for the year then ended:

- (i) an increase of inventories in the amount of approximately RMB86,696,000;
- (ii) a decrease in accounts receivable and other receivables in the amount of approximately RMB106,248,000;
- (iii) an increase of prepayments in the amount of approximately RMB97,473,000;
- (iv) an increase in short-term borrowings in the amount of approximately RMB132,533,000;
- (v) an increase in long-term borrowings in the amount of approximately RMB47,100,000;
- (vi) a decrease of accounts payable and other payables in the amount of approximately RMB51,528,000; and
- (vii) a decrease in net profit after tax for the year in the amount of approximately RMB35,361,000.

The above financial impact is subject to the review and final audit to be performed by Crowe. The Board is also working closely with Crowe to determine if a restatement of the Group's prior financial information for the year ended 31 December 2022 is required.

## LIMITATIONS

The Independent Advisor's work was conducted subject to certain limitations on the following procedures, which may have confined their procedures in identifying the full extent of facts and circumstance relating to the investigative matters. The key limitations are set out below:

1. the Independent Advisor was unable to obtain full access to the electronic documents that were stored at the server hosted by Technomash, which may contain day-to-day working files of Drilling Technology and Technomash. Since Technomash was disposed by the Group on 30 November 2023 and was no longer a subsidiary of Group when the Investigation commenced, the Independent Advisor was unable to obtain the consent from Technomash to perform computer forensic analysis on its shared drive folders. The Independent Advisor had alternatively collected, reviewed and analysed the contemporaneous working files identified at the server emails of the relevant employees of the Russian Subsidiaries.
2. In conducting computer forensic analysis and review on the server emails of Employee A, limited emails were recovered from the outbox as a result of routine deletion as explained by Employee A. As the email server of the Russian Subsidiaries has been outsourced to a third-party provider, and that the subscribed services did not include recovery of deleted emails, the Independent Advisor had alternatively reviewed and analysed the email communications between Employee A and other relevant employees whose server emails were made available to the Independent Advisor for review.
3. Three employees of the Russian Subsidiaries did not provide consent to the Independent Advisor to conduct computer forensic analysis on their computer devices, due to personal privacy concerns. The Independent Advisor had alternatively collected, reviewed and analysed their server emails.
4. The Independent Advisor was informed that Mr. Zhang Jun, Chairman of the Board and executive Director, and the General Manager of the Oilfield Equipment Segment were not assigned any corporate electronic devices. The Independent Advisor had instead collected, reviewed and analysed their server emails.



## **INTERNAL CONTROL WEAKNESS IDENTIFIED**

The Independent Advisor has identified the following internal control weaknesses of the Company:

1. insufficient oversight and awareness on the internal reporting and approval requirements for establishing special purpose entities;
2. insufficient due diligence procedures on Entity A in accordance with internal control processes during the onboarding of Entity A as an intermediary supplier;
3. no proper approval record and disclosure in relation to the Russian Guarantees;
4. lack of clear policy and procedures in relation to the definition, filing and approval process of material contracts; and
5. no proper record in relation to the declaration of conflict of interests from relevant employees.

## **OPINIONS OF THE INVESTIGATION COMMITTEE AND THE BOARD**

The Investigation Committee has reviewed the Investigation Report and accepted the key findings of the Investigation. The Investigation Committee is of the view that having taken into account the practicable limitations and making necessary enquiries with the Independent Advisor, (i) the content and the findings of the Investigation Report are reasonable and acceptable and addressed the former auditor's concerns in relation to the Transactions, (ii) the scope of the Investigation is sufficient and its limitations are reasonable; and (iii) the findings of the Investigation revealed internal control weaknesses in the Company's internal control processes which shall be addressed appropriately.

Also, the Investigation Committee is of the view that nothing has come to its attention that gives rise to concern about the integrity, competence or character of the Directors or senior management of the Company which may pose a risk to the Shareholders and potential investors or damage market confidence for the following reasons:

- (a) Although the acts of Mr. Cao and the omissions on the part of Mr. Wang Tao (汪濤), Mr. Dai and Mr. Chen Yong demonstrated insufficient sensitivity on relevant internal control processes and due diligence, there was no documentary evidence to suggest that Mr. Wang Tao (汪濤), Mr. Dai and Mr. Chen Yong had actual knowledge of the establishment of Entity A, the Transactions and related business dealings of Entity A at the relevant times or that Mr. Cao, Mr. Wang Tao (汪濤), Mr. Dai and Mr. Chen Yong had a personal interest in such matters. The Investigation Committee noted that (i) Mr. Wang Tao (汪濤) has tendered his resignation as an executive Director and chief executive officer of the Company with effect from 15 October 2024 and will cease to be a member of the nomination committee of the Company and will not hold any directorships or management positions in the Group; and (ii) Mr. Dai has tendered his resignation as the executive president of the Company with effect from 15 October 2024 and will cease to hold any directorships or management positions in the Group. Each of Mr. Cao, Mr. Wang Tao (汪濤), Mr. Dai and Mr. Chen Yong has also expressed sincere remorse and willingness to improve their knowledge in internal control and due diligence.

- (b) Based on the findings of the Investigation Report, each of the other Directors and senior management of the Company has no decision making role in the establishment of Entity A, the Transactions and related business dealings of Entity A. There was also no documentary evidence to suggest that each of the other Directors or the senior management of the Company had actual knowledge of the establishment of Entity A, the Transactions and related business dealings of Entity A at the relevant times or had a personal interest in such matters.

The Investigation Committee proposed the following recommendations which are accepted and adopted by the Board:

No.	Recommendations	Status
1.	Address findings of the Investigation Report in the audit of the Company's financial statements for the year ended 31 December 2023 and consider whether any restatement of the Group's prior financial information is needed	Findings of the Investigation Report have been provided to Crowe.
2.	Carry out necessary changes to the relevant person of the Board and the management of the Group	<ol style="list-style-type: none"> <li>1. Notwithstanding that Mr. Chen Yong had no actual knowledge of the Transactions and related business dealings of Entity A at the relevant times based on the findings of the Investigation Report, Mr. Chen shall face penalties of demerit and salary reduction.</li> <li>2. The internal audit officer of the Group has tendered his resignation as the internal audit officer of the Group with effect from 15 October 2024.</li> <li>3. Mr. Cao has tendered his resignation as the General Manager of the Oilfield Equipment Segment with effect from 15 October 2024. Mr. Cao will face penalties of demerit and salary reduction and undertake mandatory training.</li> <li>4. The vice manager of the Oilfield Equipment Segment has tendered his resignation as the vice-general manager of the Oilfield Equipment Segment and cease to hold any management positions within the Group with effect from 15 October 2024. The vice manager of the Oilfield Equipment Segment will face penalties of demerit.</li> </ol>

No.	Recommendations	Status
5.	The general manager of the Russian region has tendered his resignation as the general manager of the Russian region with effect from 15 October 2024.	
6.	The finance director of the Oilfield Equipment Segment has tendered his resignation as the finance director of the Oilfield Equipment Segment with effect from 15 October 2024. He will cease to hold any management positions in the Oilfield Equipment Segment and will no longer be responsible for financial operations thereof.	
7.	The general manager of Drilling Technology and Technomash and Employee A shall face penalty of salary reduction and receive compulsory trainings on internal control. The general manager of Drilling Technology and Technomash and Employee A will be reporting to and managed by a newly appointed general manager of the Russian region who is not previously involved in any matters concerning the Transactions, the establishment of Entity A or the Bank C Loans.	

The Investigation Committee considered the recommendations above are appropriate given that the findings of the Investigation Report show that the actions or inactions of the above persons were primarily due to an overall lack of sensitivity on internal control processes and due diligence, and that none of the persons has any ulterior intent to defraud the Company or its Shareholders.

The Company is in the process of identifying suitable candidates to fill the positions of chief executive officer of the Company, executive president of the Company and general manager of the Russian region. The Company will also appoint a qualified personnel with extensive accounting and compliance experience as the head of internal audit department, who will report directly to the Board. The head of internal audit department will be supported by qualified accounting professional. The Company aims to substantially complete the replacements by the end of November 2024.

No.	Recommendations	Status
3.	To strengthen reporting mechanisms (i) between and among each member of the senior management team and (ii) between the senior management and the Board	<p>The senior management team will hold meetings at least quarterly to discuss the latest updates on the core functions of the Group. During such meeting, all members could question and challenge each other's actions respectfully, gather and share information and offer constructive feedback. Each member, including the CEO, benefits from the insight and constructive feedback from members. This peer management mechanism at the senior management level ensures that no member has information or knowledge advantage over other members of the senior management team, and helps checks and balances of each core functions departments. Any issues identified in the senior management meeting will be raised to the Board/Board committees for further review and determination (see below).</p> <p>The heads of each business segments reports to the Board at least quarterly, which focuses on business operations and sales strategies. The CFO, the newly appointed head of internal audit department and the head of legal and compliance department collectively report to the Board at least monthly. They are closely related to “back office” responsibilities and regulatory compliance. During such meeting with the Board, no executive directors are present to ensure that directions from non-executive directors and independent non-executive directors take precedence.</p> <p>All members of the senior management team collectively hold meetings with the Board at least quarterly to report the updates on the core functions for which they are responsible, including key issues identified and subsequent resolutions to keep all parties on the same page.</p>

No.	Recommendations	Status
4.	To address the internal control weakness identified by the Independent Advisor and conduct an internal control review and rectify any weakness, including internal reporting and approval requirements, conflict on interests declaration and matters related to corporate governance, capital management and related parties management	It is expected that the findings and rectification plan of the Internal Control Review will be available around the end of October or early November 2024. The Company will immediately implement the rectification plan.
5.	To provide trainings to the management and employees of the Group on a periodic basis to improve their knowledge in accounting and the Listing Rules, including directors' responsibilities, corporate governance, notifiable and connected transactions requirements and financial reporting requirements	Relevant trainings will be provided to the management and employees of the Group regularly. It is expected that trainings of such nature will at least take place semi-annually.

Having taken into account the recommendations above, the Investigation Committee considered that the current Directors remain suitable to act as a Director under Rules 3.08 and 3.09 of the Listing Rules for the reasons set out below:

- (i) it is noted that the documentary evidence did not reveal any issues of integrity, competence or character on any current Directors;
- (ii) all the current Directors are committed to completing further training on, among others, Listing Rules compliance, director's duties and corporate governance matters; and
- (iii) all the current Directors have provided valuable contributions to the Group with their industry experience and expertise throughout his/her tenure.

The Board has reviewed the Investigation Report and concurs with the views of the Investigation Committee set out above. As of the date of this announcement, the Internal Control Review is ongoing. The Company will enhance its internal control measures and adopt recommendations proposed by the Internal Control Consultant. The Company is fully aware of the importance of maintaining the trust and confidence of shareholders, regulatory authorities and other stakeholders and the Company will ensure high standards in transparency and compliance in all respects.

## **NON-COMPLIANCE OF CHAPTER 14 OF THE LISTING RULES IN RESPECT OF THE PROVISION OF THE RUSSIAN GUARANTEES**

As disclosed in the section headed “3. Entity A’s source of funding” in this announcement, the Russian Subsidiaries and Trade House Hilong-Rus Co., Ltd. provided the Russian Guarantees in favour of Entity A to secure the Bank C Loans. Prior to the consolidation of Entity A into the Group’s accounts for FY2022 and FY2023, the Russian Guarantees, in aggregate at the relevant times, would constitute a financial assistance which is subject to reporting, announcement, circular and Shareholders’ approval requirements under Chapter 14 of the Listing Rules. As the Company did not announce, issue circular or obtain shareholders’ approval for the provision of the Russian Guarantees, the Company acknowledges that the provision of the Russian Guarantees constituted non-compliance under Chapter 14 of the Listing Rules. Given that the outstanding loan balance will be substantially reduced by the end of 2024 and fully repaid when the respective loan agreements become due, the Board (including the independent non-executive Directors) is of the view that it would not be meaningful for the Company to convene a general meeting for obtaining Shareholders’ approval for approving and ratifying the Russian Guarantees. Following the consolidation of Entity A into the Group, the Russian Guarantees over the outstanding balance of the Bank C Loans provided by Technomash, Pipeline Surgut and Pipeline Orenburg in favour of Entity A would constitute a continuing connected transaction of the Company under Chapter 14A of the Listing Rules. Given that the financial assistance received by the Group from these connected persons was conducted on normal commercial terms or better and was not secured by the assets of the Group, it would be fully exempt under Rule 14A.90 of the Listing Rules.

To prevent the occurrence of any similar incidents in the future, the Group will arrange trainings for the management and employees of the Group on a periodic basis in relation to notifiable and connected transactions of the Listing Rules and seek advice from external professional advisors from time to time as appropriate. The Group will also implement the rectification plan of the Internal Control Review.



## CONTINUED SUSPENSION OF TRADING

At the request of the Company, the trading in the shares of the Company on the Stock Exchange has been suspended from 9:00 a.m. on 2 April 2024, and will remain suspended until further notice.

**Shareholders and potential investors of the Company are advised to exercise due caution when dealing in the securities of the Company. When in doubt, Shareholders and potential investors of the Company are advised to seek advice from their own professional or financial advisers.**

For and on behalf of the Board  
**Hilong Holding Limited**  
**ZHANG Jun**  
*Chairman*

Hong Kong, 16 October 2024

*As at the date of this announcement, the executive director of the Company is Mr. ZHANG Jun; the non-executive directors are Ms. ZHANG Shuman, Dr. YANG Qingli, Mr. CAO Hongbo and Dr. FAN Ren Da Anthony; and the independent non-executive directors are Mr. WANG Tao (王濤), Mr. WONG Man Chung Francis and Mr. SHI Zheyang.*

\* *For identification purpose only*