

**IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF FIRST INSTANCE
MISCELLANEOUS PROCEEDINGS NO 868 OF 2019**

IN THE MATTER OF Sound Global
Limited

and

IN THE MATTER OF Section 214 of
the Securities and Futures Ordinance
(Cap. 571)

BETWEEN

SECURITIES AND FUTURES COMMISSION

Petitioner

and

SOUND GLOBAL LTD. (桑德國際有限公司)

1st Respondent

WEN YIBO (文一波)

2nd Respondent

ZHANG JINGZHI (張景志)

3rd Respondent

WANG KAI (王凱)

4th Respondent

ZHANG XIQUAN (張希泉)

5th Respondent

Before: Hon Linda Chan J in Court

Dates of Hearing: 14 – 17, 23 June 2022

Date of Judgment: 30 September 2022

J U D G M E N T

1. This is the trial of the petition presented by the Securities and Futures Commission (“SFC”) on 14 June 2019 (as amended on 13 September 2019) (“**Petition**”) under s.214 of the Securities and Futures Ordinance (Cap. 571) (“SFO”) against *inter alios* Sound Global Ltd (“**Company**”) and Mr Wen Yibo (“**Mr Wen**”), who are respectively the 1st and 2nd respondents named in the Petition.

2. In the Petition, the SFC seeks:

- (1) a disqualification order¹ against Mr Wen and an order requiring him to purchase the shares of the Company from the other members at a price to be determined by the court;² and/or
- (2) an order directing the Company to appoint an independent external auditor to review and prepare a report on its internal control and finance reporting procedures, and to publish and implement such suggested measures.

A. *PROCEDURAL MATTERS*

3. The 3rd to 5th respondents, who were former directors of the Company, are residents in the Mainland. Despite having obtained leave to serve the Petition on the 3rd to 5th Respondents in the Mainland pursuant to

¹ Under SFO s.214(2)(d) or s.214(2)(a).

² Under SFO s.214(2)(e).

Order 11 rule 5A of the Rules of the High Court on 12 September 2019, and the repeated attempts by the relevant judicial authorities to effect service, the Petition has not been served on such respondents. The SFC decides to proceed with the trial against Wen and the Company only.

Al. No Case Management Hearing before Trial

4. Upon the joint application of the SFC and Mr Wen by way of a consent summons, on 6 October 2020, Mr Recorder Pow SC gave *inter alia* the following directions (collectively “**Directions**”):

- (1) Leave to the SFC to fix the substantive hearing of the Petition before a bilingual Judge in consultation with counsel’s diaries with 8 days reserved (§1);
- (2) In the event that the court makes an order requiring Mr Wen to purchase the shares of the Company from public shareholders, further directions shall be given in respect of (a) the filing of expert evidence for determining the price of the shares to be purchased and (b) the substantive hearing of such issue (§2);
- (3) The deponent of the affirmations shall attend the substantive hearing for cross-examination failing which their affirmations shall not be admitted as evidence. Unless otherwise directed by the trial judge, the affirmations shall stand as evidence in chief (§§5-7); and
- (4) Subject to §7 (which requires the deponents to attend the trial for cross-examination), all exhibits (including the records of

interviews (“**ROIs**”)) to the affidavits / affirmations shall be admitted as evidence at the substantive hearing (§8).

5. The parties proceeded to fix the date for the trial. None of the parties brought the Petition to the court for further directions at a case management conference or pre-trial review. Consequently, the court did not have the opportunity to consider questions relevant to the fair disposal of the Petition including:

- (1) whether the Company should take an active step or incur any legal costs in the proceedings;
- (2) whether there is a proper basis to fix the trial before a bilingual judge;
- (3) whether it is cost-effective and a proper use of judicial resources for the court to hear a trial which only involves 2 out of the 5 respondents;
- (4) whether it is appropriate to admit the ROIs as evidence without requiring the interviewees to attend trial for cross-examination;
- (5) whether the SFC will call any of the interviewees to attend trial for cross-examination;
- (6) whether Mr Wen intends to cross-examine any of the interviewees, which has a bearing on the length of trial; and
- (7) the time table, directions on trial bundles and the documents to be submitted for trial.

6. Had the parties pursued the Petition in the same way as a petition concerning a company³, the court would have required the parties to address the aforesaid questions and give appropriate directions at an early stage. In particular:

(1) The Petition is brought by the SFC to redress the wrongs allegedly done to the Company and the relief is sought for the benefit of the Company. It is difficult to see why the Company should incur legal costs in filing affirmation in response to the Petition and engaging solicitors and counsel to appear at trial.

(2) It does not appear that there is any basis for the Petition to be fixed before a bilingual judge. Given the prevalence of companies whose shares are listed on The Stock Exchange of Hong Kong Limited (“SEHK”) with businesses and investments located in the Mainland, it is inevitable that most of the documentary and oral evidence concerning these companies are in Chinese. The savings in time and costs involved in translating documents and evidence *per se* are not sufficient justifications for the matter to be fixed before a bilingual judge. It is also wrong for the parties to assume that if the matter is to be heard before a bilingual judge it would not be necessary to translate the documents essential to their case. This is particularly so when the substantive hearing is to be conducted in English and without translation, the judge

³ Which is governed by PD 3.4 Case Management for Bankruptcy Petitions, Winding-up Petitions and Petitions under section 724 of the Companies Ordinance.

will have to do his/her own translation when it comes to writing judgment.

(3) It does not seem to me that there is any justification for the SFC not to ask its witnesses to prepare and adduce affirmations as evidence. While it may be convenient and cost-effective for the SFC to adduce ROIs as evidence, when it comes to trial, many of the answers recorded in the ROIs are no longer relevant to the issues between the parties. It is also unfair to require the respondents and the court to trawl through voluminous ROIs to ascertain which parts are relevant to the issues or will be relied on by the SFC at trial.

(4) The SFC has not identified the basis for asking the court to give a special status to ROIs or why the court's hands should be tied in the manner suggested in §8 of the Directions. As ROIs are not affidavits or affirmations, §7 of the Directions (which require the deponents to attend trial for cross-examination) does not apply. §8 states that ROIs shall be admitted as evidence at trial, but the question of admissibility of evidence is a matter for the court.

7. It was only when the parties applied by consent on 19 April 2022 for an extension of time to comply with some of the Directions that on 22 April 2022, this Court gave the usual directions requiring the parties to file trial bundles, Agreed List of Issues, Statement of Agreed Facts, Agreed Chronology and Agreed Dramatis Personae and Abbreviations for use at trial. As for the other issues identified in §5 above, the position of the SFC is as follows:

- (1) Unless there is any change of circumstances, the SFC does not envisage that it will pursue the Petition against the 3rd to 5th respondents;
- (2) The SFC has procured 4 interviewees to attend trial for cross-examination (see §10(1)-(4) below); and
- (3) There are 7 interviewees whose ROIs are in the trial bundles but will not attend trial for cross-examination (see §12 below). The SFC adduces their ROIs as hearsay evidence, and accepts that it is for the court to decide what weight should be given to such ROIs.

A2. Role of the Company

8. The Company engaged Messrs. Stevenson, Wong & Co (“SWC”) and counsel Mr Thomas WK Wong to attend trial. In his Opening, Mr Wong stated that the Company “does not contest” the relief sought in §3 of the prayer and “stays neutral” to the rest of the Petition. He points to the Affirmation of Feng Ji (“**Mr Feng**”) dated 24 December 2019 filed on behalf of the Company (“**Feng 1st**”) and submitted that the Company “is not in a position to confirm / agree” to the various facts stated in the Statement of Agreed Facts because (1) the relevant financial records had been destroyed in fire; (2) the relevant banks had not responded to letters of enquiry or could not print out bank statements for the relevant period; and (3) the relevant personnel had left the Company and were untraceable.

9. On the first day of trial, this Court observed that the allegations made by the SFC are all directed against the 2nd to 5th

respondents, who are former directors of the Company, and the relief is sought for the benefit of the Company. As the Company is neutral and does not seek to cross-examine any of the witnesses or make any submissions on the relief sought in the Petition, it is not clear why the directors considered that it would be in the interests of the Company to engage SWC and counsel to attend trial. If the court is not satisfied that the attendance of solicitors and counsel at trial is necessary for the fair disposal of the Petition, it may consider ordering the costs incurred by the Company to be paid by the directors. Before the commencement of Day 2 of trial, SWC confirmed that they would not attend the remaining days of trial unless otherwise directed by the court.

A3. Factual Witnesses

10. The SFC called the following factual witnesses:

(1) Ms Wang Linlin Freya (“**Ms Wang**”) of Deloitte Touche Tohmatsu Certified Public Accountants LLP, Beijing office (“**Deloitte BJ**”). She was interviewed by the China Securities Regulatory Commission (“**CSRC**”) in Beijing on 26 April 2017 and her answers were recorded in ROI of the same date. From October 2013 onwards, Ms Wang performed audit work in relation to the bank accounts, fixed assets and sales management fees of the companies within the “Group” (as defined in §12(4) below) as part of the audit on the consolidated financial statements of the Group for the year ended 31 December 2013 (“**2013 AFS**”) and.

(2) Mr Yu Man To Gerald Maximillian (“**Mr Yu**”), the Chief Financial Officer (“**CFO**”) and Joint Company Secretary of

the Company from 21 June 2011 to 28 February 2013. He was interviewed by the SFC on 18 May 2017 and his answers were recorded in ROI of the same date.

(3) Mr Seow Han Chiang Winston (“**Mr Seow**”), an Independent Non-Executive Director (“**INED**”) of the Company from 24 August 2006 to 13 July 2015. Mr Seow is a qualified lawyer and practices in merger, acquisition and corporate matters. He was interviewed by the SFC on 13 March 2017 and his answers were recorded in ROI of the same date.

(4) Mr Wong See Meng (“**Mr Wong**”), an INED of the Company from 19 May 2009 and 26 March 2015 during which he acted as Chairman of the Audit Committee. He has always been based in Singapore. He was interviewed by the SFC on 19 May 2017 and his answers were recorded in ROI of the same day.

(5) Mr Cheng Tak Ka (“**Mr Cheng**”), an associate director of the enforcement division of the SFC. He made an affirmation dated 14 June 2019 (“**Cheng 1st**”) and a 4th Affirmation dated 6 February 2020 in support of the Petition.

11. Amongst them, Mr Cheng and Mr Yu gave *viva voce* evidence in court, while Mr Seow, Mr Wong and Ms Wang gave evidence via VCF. They adopted their ROIs as evidence in chief. Ms Tara Liao, counsel for Mr Wen, only cross-examined Mr Cheng briefly.

A4. ROIs

12. In addition, the SFC adduced the ROIs of the following 7 persons without calling them to give oral evidence at trial:

(1) Ms Susan Su Xiulan (“**Ms Su**”), formerly a staff of Deloitte BJ. She was interviewed by the CSRC on 25 April 2017 and her answers were recorded in ROI of the same day.

(2) Ms Viola Fang Junqiu (“**Ms Fang**”), a former staff of Deloitte BJ. She was interviewed by the CSRC on 26 April 2017 and her answers were recorded in ROI of the same date.

(3) Ms Maggie Yu Han (“**Ms Yu**”), formerly a staff of Deloitte BJ. She was interviewed by the CSRC on 26 April 2017 and her answers were recorded in ROI of the same date.

(4) Mr Li Fajun (“**Mr Li**”), contact person and relationship manager of the Company and its subsidiaries (together “**Group**”) who worked at Chegongzhuang branch of Hua Xia Bank (“**HXB**”) at the material time. He was interviewed by the CSRC on 25 April 2017 and his answers were recorded in ROI of the same date.

(5) Ms Huang Qiong (“**Ms Huang**”), accounting manager of Chegongzhuang branch of HXB. She was interviewed by the CSRC on 16 June 2017 and her answers were recorded in ROI of the same date.

(6) Ms He Hufeng (“**Ms He**”), contact person and relationship manager for the Group at Zhongguancun branch of Ping An Bank (“**PAB**”) at the material time. She was interviewed by

the CSRC on 25 April 2017 and her answers were recorded in ROI of the same date.

(7) Ms Dong Junyu (“**Ms Dong**”), internal control manager of Zhongguancun branch of PAB. She was interviewed by the CSRC on 6 June 2017 and her answers were recorded in ROI of the same date.

13. Mr Jenkin Suen SC (leading Ms Sheena Wong), counsel for the SFC, explained that the reasons for not calling the aforesaid 7 interviewees to give *viva voce* evidence were: (1) Ms Su, Ms Fang and Ms Yu were no longer employed by Deloitte BJ; (2) Mr Li and Ms He were implicated in the wrongdoings complained of in the Petition⁴; and (3) Ms Huang and Ms Dong were colleagues of Mr Li and Ms He at the respective branches, and they showed reluctance to give evidence in these proceedings. Given that the explanations were only provided at trial, the matter could not properly be explored.

14. Mr Suen submitted that ROIs are hearsay evidence and the parties have agreed to their admissibility (as reflected in §8 of the Directions). There is no ground for excluding the ROIs under s.47(1) of the Evidence Ordinance (Cap. 8). Nor is there any rule against admitting ROIs in s.214 proceedings, for eg., *SFC v Cheung Keng Ching & ors*, HCMP 1869/2008, 18 March 2010, §§10, 21, 41(3) & 41(5) per Burrell J; and the appeal therefrom [2011] 4 HKC 453, §§18(5) & 18(7) per Fok JA. Insofar as the court finds it appropriate to rely on such ROIs, it may have regard to the considerations as to weight as set out in s.49 of the Evidence Ordinance (Cap. 8).

⁴ Petition §48.

15. I am unable to accept the approach of the SFC:

- (1) The proceedings in *SFC v Cheung Keng Ching* were disposed of summarily by way of *Carecraft* procedure. The court did not need to consider any disputed evidence of facts or make any findings for such purpose. There was no discussion on any of the questions concerning the use of ROIs including those identified in §5(4) above.
- (2) The directions in *SFC v Cheung Keng Ching* (relied on by Mr Suen), which allowed the company to use the affirmations, statements, ROIs and other documents filed or disclosed by the parties in the s.214 proceedings in the civil proceedings to be commenced⁵ against the 1st to 3rd respondents (former directors of the company against whom the court made the disqualification orders), were made in the context of the court having ordered the company to commence civil proceedings against such respondents to seek recovery or compensation for the loss suffered. The court made clear that the questions of admissibility and weight of such evidence are matters for the court hearing the civil proceedings.
- (3) It was for the SFC (not the court) to identify which specific parts of ROIs it relied on, so that Mr Wen could decide whether to dispute their contents. The SFC could then make submissions on what weight should be given to those ROIs, taking into account their relevance, probative value and the

⁵ Which was necessary given that the parties were bound by the implied undertaking not to use any documents obtained under compulsory powers in the proceedings for a collateral purpose including other legal proceedings.

reasons for not calling the interviewees to attend trial to give oral evidence.

16. Mr Suen confirmed that the SFC mainly relied on those ROIs referred to in footnotes 4 and 5 to his written Closing. The ROIs identified in footnote 4 relate to the answers given by the staff of HXB and PAB where they said that they had not seen the “Company’s Records” (as defined in §39 below). Those answers were in very general terms and not sufficient to prove that the Schemes had been perpetrated. However:

(1) The SFC has adduced *all* the records of the “8 Bank Accounts” (as described in §39(2) below) for the period from 2012 to 2015 obtained by the CSRC from HXB and PAB (collectively “**CSRC’s Records**”) as documentary evidence. The CSRC’s Records did *not* include all the documents within the Company’s Records for the same period. This confirms the fact that the Company’s Records, to the extent that they cannot be found in the CSRC’s Records, were not genuine records of the 8 Bank Accounts generated by PAB and HXB but were fictitious documents.

(2) Although Ms Liao in her written Opening attempted to challenge the authenticity of the CSRC’s Records, I do not think that she was entitled to do so given that Mr Wen had not disputed the authenticity of the CSRC’s Records in Wen 1st or filed any notice of non-admission for such purpose.

A5. Mr Wen and Mr Feng's evidence

17. Mr Wen adduced his affirmation dated 17 December 2019 (“**Wen 1st**”) as evidence. He gave evidence through VCF and was cross-examined by Mr Suen for 2 days. Although in Wen 1st he denied many of the allegations raised in the Petition, under cross-examination, Mr Wen admitted that (a) the CSRC’s Records are authentic; (b) there were material discrepancies in the Company’s Records and some of the bank statements and bank confirmations provided by the Company were false; and (c) such discrepancies were one of the problems which the Group had tried to investigate.

18. Mr Feng is and has since October 2017 been the assistant to Chairman and general manager of the securities department of the Company. Mr Feng was cross-examined by Mr Suen. It is clear from his answers that he was not involved in, nor did he have any personal knowledge of, the transactions complained of in the Petition as they all predated his employment by the Company. Mr Feng’s evidence is no more than his subjective belief or re-construction of past events based on the documents available to him. I do not think that there is any probative value in Mr Feng’s evidence.

B. FACTUAL BACKGROUND

19. The following facts are not in dispute or are based on documents which are not disputed.

B1. The Company and Management

20. The Company is an investment holding company. Its shares have since 30 September 2010 been listed on the Main Board of SEHK (stock code: 967).⁶ The Company's shares were also listed on the Singapore Stock Exchange between 6 October 2006 until its voluntary delisting on 27 January 2014.⁷

21. On 13 April 2016, trading in the Company's shares was suspended pursuant to rule 8(1) of the Securities and Futures (Stock Market Listing) Rules and has not resumed to-date.⁸

22. The Company through its subsidiaries in the Mainland carries on business in turnkey water and wastewater treatment. It has offices in Hong Kong, Singapore and Beijing.⁹

23. The Company has 3 indirect wholly owned subsidiaries which accounted for a significant part of the assets and revenue of the Group namely: (1) Beijing Epure International Water Co Ltd ("**BJ Epure**"), (2) Beijing Sound Environmental Engineering Co Ltd ("**BJ Sound**"), and (3) Beijing Hi-Standard Water Treatment Equipment Co Ltd ("**BJ Hi-Standard**") (collectively "**Subsidiaries**").

24. Mr Wen is the founder of the Group and an executive director ("**ED**") and Chairman of the Company from 7 November 2005.¹⁰ He is the controlling shareholder of the Company holding at least 50% of its issued

⁶ Petition §§2, 10.

⁷ Petition §10.

⁸ Petition §36.

⁹ Petition §2.

¹⁰ Petition §12(1).

shares. As at 31 December 2013, Mr Wen held an effective 55.31% shareholding in the Company.¹¹ He was a director of each of the Subsidiaries and the sole or one of the authorised signatories of the 8 Bank Accounts at the time of the transactions complained of in the Petition.

25. The other members of the senior management of the Company at the times of the impugned transactions included:

(1) Mr Zhang Jingzhi (“**R3**”) who joined the Group in April 2001. He was an ED and Chief Executive Officer (“**CEO**”) of the Company from 4 March 2013 to 11 August 2016.¹²

(2) Mr Wang Kai (“**R4**”) who joined the Group in 1998. He was appointed an ED of the Company on 24 December 2010. He was CEO from 2 February 2011 to 3 March 2013, and CFO from 4 March 2013 to 17 December 2015.¹³

(3) Mr Zhang Xiquan (“**R5**”) who joined the Group as an accountant in September 2003. He was vice general manager of the finance department from March 2008 to July 2011, and was general manager and head of the finance department at the Group’s office in Beijing from August 2011 to 13 April 2016.¹⁴

¹¹ Petition §12(1).

¹² Petition §12(2).

¹³ Petition §12(3).

¹⁴ Petition §12(6).

B2. 2012 AFS and 2013 AFS

26. Deloitte Touche Tohmatsu Certified Public Accountants LLP (“**Deloitte**”) were the auditors of the Company from 2008 until its resignation on 17 July 2015.

27. On 22 March 2013, the Company published its 2012 Annual Report together with the audited consolidated financial statements of the Group for the year ended 31 December 2012 (“**2012 AFS**”).

28. On 11 April 2014, the Company published its 2013 Annual Report together with 2013 AFS.

29. The 2012 AFS and 2013 AFS were audited by Deloitte.

30. In the 2012 AFS and 2013 AFS, the Company represented to its shareholders and the public that the Group had (1) capital and reserves and (2) bank balances and cash in the following amounts:

	As at 31.12.2011 RMB	As at 31.12.2012 RMB	As at 31.12.2013 RMB
Capital and reserves	2,304,669,000	2,654,512,000	3,074,291,000
Bank balances and cash	2,074,426,000	2,912,077,000	3,533,547,000
Increase in bank balance and cash		837,651,000	621,470,000

B3. Emerson Reports and SFC's investigations

31. On 4 and 16 February 2015, Emerson Research Analysts Co, an equities research firm, issued 2 reports in relation to the Company (together “**Emerson Reports**”) which suggested that:

- (1) BJ Epure had purportedly supplied the Company with about RMB 1 billion of false revenue in technology services, and BJ Epure was a shell company used for booking such revenue;
- (2) There was evidence to suggest that the 2013 revenue from its Anshan plant had been fraudulently inflated by RMB 380 million;
- (3) The Group’s true cash and bank balances likely averaged only one third of the amounts reported; and
- (4) The real profitability of the Group in 2013 was only slightly more than a quarter of the amount reported.

32. In response to the Emerson Reports, the Company issued clarifications on 13, 17 and 24 February 2015.

33. The SFC was concerned about whether false or misleading information had been disclosed or provided by the Company.¹⁵ On 16 March 2015, the SFC issued a notice under s.183 of the SFO (“**s.183 Notice**”) requiring the Company to produce (*inter alia*) bank statements and information relating to the Group’s bank balances and cash positions as at 31 December 2012 and 31 December 2013.¹⁶

¹⁵ Petition §22.

¹⁶ Petition §38.

B4. 2015 Cash Discrepancy

34. On 10 March 2015, a representative of the Company (Mr Si Zhiqiang) visited the Chegongzhuang branch of HXB together with representatives of Deloitte to confirm the Group's bank account balances for the year ended 31 December 2014. During the visit, Deloitte discovered that there was a discrepancy of around RMB 2 billion between the balances in the Group's bank accounts at HXB and the information previously provided by the management ("**2015 Cash Discrepancy**").¹⁷

35. At that time, the existence of the 2015 Cash Discrepancy was not in dispute:

(1) At the meeting held on 10 March 2015 between Deloitte and the Company's audit committee¹⁸ and during a telephone conversation with Deloitte, R5 acknowledged that there were discrepancies between the bank balances previously provided to Deloitte and the Group's actual balances.

(2) At the meeting between Deloitte, Mr Wen and R5 on 11 March 2015, Mr Wen acknowledged the existence of the 2015 Cash Discrepancy, and said that RMB 2 billion cash had been used by him for his other businesses ("**1st Explanation**").

(3) By letter dated 12 March 2015 addressed to the board and the audit committee of the Company, Deloitte drew their attention to the 2015 Cash Discrepancy, and stated that (a) there were "[s]ignificant governance, internal control and financial reporting and regulatory concerns" regarding the Company's

¹⁷ Petition §§23-30.

finances; (b) the board should take steps to “prevent continuing reliance on the Group’s financial reports in the public domain”; (c) Mr Wen and R5 should make full disclosure of the facts, including the precise amount of the Group’s missing cash and whether such amount was recoverable by the Group; (d) the audit committee should obtain bank statements from all the banks used by the Group; and (e) the audit committee should consider the need to suspend the directors from participation in the financial reporting process.

(4) Also on 12 March 2015, Mr Wen met with and informed the audit committee that: (a) he was responsible for the 2015 Cash Discrepancy; (b) he had taken and used RMB 2 billion for his own investments; and (3) the amount had not been returned to the Group, but he would find the means to return the money as soon as possible.

(5) On 16 March 2015, trading of the shares was suspended. At the meeting between the INEDs and Deloitte’s representatives, Mr Wen was urged to meet and cooperate with the audit committee, and the audit committee must ascertain from Mr Wen whether there was any other shortfall in the Group’s bank balances apart from the 2015 Cash Discrepancy.

(6) At the board meeting of the Company held on 19 March 2015, Mr Wen acknowledged the existence of the 2015 Cash Discrepancy but put forward a different explanation. He said RMB 2 billion had been used in the second half of 2014 in negotiating several acquisitions carried on by his associated

companies on behalf of the Group as it was inconvenient to involve the Company due to the scale of the acquisitions. The matter was discussed with R3 and R4, and it was decided that Mr Wen's associated companies would be used for such purpose. The negotiations fell through but the funds had not yet been repaid to the Company ("**2nd Explanation**").

- (7) Further board and audit committee meetings were held on 20 March and 26 March 2015 to discuss the 2015 Cash Discrepancy at which R4 reported the status of obtaining bank statements from the Group's 6 largest banks and further enquiries to be made with other banks.

B5. Investigations by PKF and RSM

36. On 23 June 2015, the Company announced that PKF Accountants & Business Advisors ("**PKF**") engaged by the independent review committee of the Company to review the 2015 Cash Discrepancy, reported that the said Discrepancy was the result of:

- (1) the Company having paid RMB 2 billion as earnest money for a proposed acquisition of 2 Chinese water treatment companies ("**Proposed Acquisitions**") through Sound Group Co Ltd ("**SGC**"), a company held by Mr Wen and his wife; and
- (2) the payment had not been recorded in the Group's bank accounts in a timely manner.¹⁹

¹⁹ Petition §31.

37. In the further announcement dated 31 August 2015, the Company stated that RSM Corporate Advisory (Hong Kong) Limited (“RSM”) had conducted forensic investigations into the 2015 Cash Discrepancy²⁰. In its report dated 20 November 2015, RSM stated that PKF’s findings were consistent with the Company’s explanation that the 2015 Cash Discrepancy was due to the earnest money paid through SGC as its agent for the Proposed Acquisitions, which transactions had been omitted from the Company’s accounting records.²¹ In particular, RSM reported that:

- (1) According to its confirmation results, RMB 2 billion was paid by SGC on behalf of the Group in that: (a) on 4 November 2014, RMB 600 million was paid to Changye Environ Prot. Group on behalf of BJ Sound; (b) on 24 November 2014, RMB 530 million was paid (on behalf of BJ Sound), and RMB 870 million was paid (on behalf of BJ Epure), both to Dongda Group Co Ltd.
- (2) None of the aforesaid payments were recorded in the accounts of BJ Sound, BJ Epure or the Group until 3 April 2015.
- (3) By a supplemental agreement dated 20 March 2015, SGC agreed to transfer RMB 2 billion (together with interest) back to the Company’s bank accounts within 1 month.
- (4) On 13 April 2015, SGC repaid RMB2 billion to the Group of which RMB 870 million was paid into BJ Epure’s account

²⁰ Petition §33.

²¹ Petition §§32, 34.

with China Merchants Bank and RMB1.13 billion into BJ Sound's account with Bank of China.

38. In light of RSM's findings, SEHK did not pursue the matter further, and trading in the Company's shares resumed on 25 January 2016.²²

B6. Company's Records v CSRC's Records

39. Meanwhile, in response to the s.183 Notice, on 13 July 2015 and 4 August 2015, the Company through its solicitors, Messrs. Brandt Chan & Partners ("**BCP**") provided to the SFC (1) some excel tables setting out the Group's bank details,²³ and (2) copies of the Group's bank statements for the years 2012 and 2013²⁴ ("**Company's Records**") which, on their face, showed that:

(1) The bank balance of the Group was RMB 2,992,785,280 as at 31 December 2012, and RMB 3,643,039,301 as at 31 December 2013; and

(2) The Group had over 200 bank accounts, of which the following 8 accounts maintained by the Subsidiaries at HXB and PAB (collectively "**8 Bank Accounts**") accounted for 75% of the Group's balance as at 31 December 2012 and 77% as at 31 December 2013²⁵:

²² Petition §35.

²³ Petition §39.

²⁴ Petition §39.

²⁵ Petition §§39-40.

		Account no.	As at 31.12.2012 RMB	As at 31.12.2013 RMB
HXB	BJ Epure	10282000000392483 ("483")	36,363,637	302,726,462
	BJ Sound	4066200001801500001551 ("551")	553,252,948	785,393,392
	BJ Sound	10282000000448756 ("756")		30,000,000
	BJ Hi- Standard	4066200001819100006105 ("105")	120,971,866	90,925,102
PAB	BJ Epure	11008393782501 ("501")	1,089,049,992	994,904,877
	BJ Sound	11000951057002 ("002")	433,281,406	571,497,631
	BJ Sound	18000951057001 ("001")	10,000,000	27,000,000
	BJ Hi- Standard	11009345733702 ("702")	4,207	4,223
Total			2,242,924,055	2,802,451,687
Bank balance in all Group's bank accounts			2,992,785,281	3,643,039,301
% held in 8 Bank Accounts			75%	77%

B7. CSRC's Records

40. On 25 March 2016 and 12 August 2016, the SFC received from CSRC the bank records of the 8 Bank Accounts for the period from 2012 to 2015²⁶. The CSRC's Records were obtained from PAB and HXB.

C. ISSUES

41. It is the SFC's case that:

- (1) The Group's financial position in the 2012 AFS and 2013 AFS had been falsely and substantially inflated as a result of the

fictitious balances in the 5 out of the 8 Bank Accounts maintained by the Subsidiaries.

(2) Mr Wen knowingly caused, directed and/or orchestrated a scheme for (a) the fraudulent inflation and falsification in the Subsidiaries' bank balances at HXB and PAB for the financial years of 2011, 2012 and 2013 ("**Falsification Scheme**") and/or (b) the fabrication of falsified bank statements and bank balance confirmations to support the inflated and fictitious bank balances ("**Fabrication Scheme**") (collectively "**Schemes**").

(3) Alternatively, Mr Wen:

(a) knew or turned a blind eye to the Schemes and did not report the same to other members of the Company's board of directors, shareholders, auditors and/or the regulatory authorities;

(b) took active steps to conceal the Schemes and to mislead other members of the board of directors, shareholders, auditors and/or the regulatory authorities; and/or

(c) acted negligently and/or in breach of his duties of skill, care and diligence owed to the Company.²⁷

(4) Further, Mr Wen knowingly gave false and/or misleading explanations regarding the 2015 Cash Discrepancy to *inter alios* RSM, the independent accountants appointed by the

²⁷ Petition §9.

Company to investigate the issue, the Company's auditors, board of directors and/or members.

(5) By reason of the above matters, the business and affairs of the Company were conducted by Mr Wen in a manner:

(a) involving defalcation, misfeasance or misconduct towards the Company, its subsidiaries and its members (s.214(1)(b));

(b) resulting in its members not having been given all the information with respect to its business or affairs that they might reasonably expect (s.214(1)(c)); and/or

(c) which was unfairly prejudicial to its members or part of its members (s.214(1)(d)).²⁸

42. Ms Liao's in her Opening and Closing made much submission on the SFC's pleaded case and the evidence adduced and argued that they fell short of the standard and cogency commensurate with the serious nature of the allegations. While it is correct that the burden is on the SFC to prove its allegations with cogent evidence, one cannot lose sight of the fact that under cross-examination, Mr Wen no longer disputed the existence of the "2012 Discrepancy" (as defined in §47(1) below), the "2013 Discrepancy" (as defined in §47(2) below) (together "**Discrepancies**") and the 2015 Cash Discrepancy. Rather, his case is that:

(1) he was not involved in and had no knowledge of the Discrepancies;

²⁸ Petition §89.

(2) he did not deliberately provided a false explanation for the 2015 Cash Discrepancy; and

(3) he acted honestly and reasonably by taking reasonable steps to investigate the Discrepancies and the 2015 Cash Discrepancy after they had been uncovered including appointing PKF and RSM to investigate them.

43. As for relief, Ms Liao argued that:

(1) No disqualification order should be made against Mr Wen as he did not act in breach of duties owed to the Company;

(2) Even if the court finds that Mr Wen was negligent in allowing the Schemes to take place or that he participated in the Schemes, the disqualification should be within the middle bracket of 6-10 years given that no financial loss has been suffered by the Company and Mr Wen did not derive any benefit from the Schemes; and

(3) There is no justification for the court to order Mr Wen to buy out the shares held by other members.

44. Accordingly, the issues which require determination by the court are as follows:

(1) whether the financial position of the Group in the 2012 AFS and 2013 AFS had been inflated as a result of the Falsification Scheme and/or the Fabrication Scheme (1st Issue);

- (2) whether Mr Wen knowingly caused, directed and/or orchestrated the Falsification Scheme and/or the Fabrication Scheme (2nd Issue);
- (3) alternatively, whether Mr Wen took a blind eye to the Schemes (3rd Issue);
- (4) alternatively, whether Mr Wen acted in breach of his duty of skill, care and diligence owed to the Company in allowing the Schemes to be perpetrated against the Subsidiaries and the Group (4th Issue);
- (5) whether Mr Wen gave false or misleading explanations regarding the 2015 Cash Discrepancy to RSM, Deloitte, the board and members of the Company and/or took steps to conceal the Schemes from other members of the board, members, auditors and the regulatory authorities (5th Issue);
- (6) whether if the aforesaid matters (or any of them) are established, the business and affairs of the Company were conducted by Mr Wen in a manner within the meaning of s.214(b), (c) and (d) of the SFO (6th Issue); and
- (7) if the transactions complained of by the SFC are established, whether the court should grant the relief sought against the Company and Mr Wen (7th Issue).

45. I consider the issues in turn.

D. DISCUSSION

D1. 1st Issue: whether 2012 AFS & 2013 AFS were inflated

46. The evidence proving the existence of the Falsification Scheme and the Fabrication Scheme is overwhelming.

47. First, a comparison of the CSRC's Records (which are indisputable for the reasons stated in §16 above) and the Company's Records shows that there were the following discrepancies in 5 out of the 8 Bank Accounts (collectively "**5 Bank Accounts**")²⁹:

- (1) As at 31 December 2012, a discrepancy of RMB 2.18 billion ("**2012 Discrepancy**")³⁰:

		Bank Accounts	Per CSRC's Records (RMB)	Per Company's Records (RMB)	Discrepancy (RMB)
HXB	BJ Epure	483	0	36,363,637	(36,363,637)
	BJ Sound	551	17,369,185	553,252,948	(535,883,763)
	BJ Hi- Standard	105	4,463,422	120,971,866	(116,508,444)
PAB	BJ Epure	501	20,622	1,089,049,992	(1,089,029,369)
	BJ Sound	002	30,438,634	433,281,406	(402,842,771)
Total			52,291,863	2,232,919,848	(2,180,627,985)

- (2) As at 31 December 2013, a discrepancy of RMB 2.72 billion ("**2013 Discrepancy**"):

²⁹ Petition §42.

		Bank Accounts	Per CSRC's Records (RMB)	Per Company's Records (RMB)	Discrepancy (RMB)
HXB	BJ Epure	483	8,905	302,726,462	(302,717,557)
	BJ Sound	551	20,003,847	785,393,392	(765,389,545)
	BJ Hi- Standard	105	425,049	90,925,102	(90,500,053)
PAB	BJ Epure	501	9,317	994,904,877	(994,895,560)
	BJ Sound	002	18,451	571,497,631	(571,479,180)
Total			20,465,568	2,745,447,464	(2,724,981,896)

48. In other words, through the Company's Records, the Subsidiaries had created fictitious bank balances in the 5 Bank Accounts in the amount of RMB 2.18 billion and RMB 2.72 billion as at 31 December 2012 and 2013 respectively³¹. The discrepancies were very significant in that they represented 82% and 89% of the net assets of the Group as at 31 December 2012 and 2013.

49. Second, it is the unchallenged evidence of Ms Wang (a staff of Deloitte BJ) that the Company's Records had been provided to and relied upon by Deloitte as evidence confirming the existence of the bank balances stated in the 2012 AFS and 2013 AFS.³²

50. Third, the undisputed evidence shows that the Fabrication Scheme was carried out in the following manner³³:

³¹ Petition §44.

³² Petition §41; Ms Wang's ROI.

³³ Petition §§50-58; Cheng 1st §§41-44; Ms Huang's ROI; Ms Dong's ROI; Mr Li's ROI; Ms He's ROI; Ms Wang's ROI; Ms Su's ROI; Ms Fang's ROI; Ms Yu's ROI; RSM Report §24.

(1) Member(s) of senior management provided or caused to be provided to Deloitte fabricated bank statements and false information pertaining to the 5 Bank Accounts.

(2) In reliance on such fabricated bank statements and false information, Deloitte prepared and issued bank confirmation forms in respect of the balances of the 5 Bank Accounts as shown in the fabricated bank statements.³⁴

(3) The bank confirmation forms were sent by Deloitte to PAB and HXB for completion. However, officers of PAB and HXB (including Mr Li of HXB, and Ms He of PAB) intervened and bypassed normal confirmation procedures and issued the confirmation forms without the banks' authority, and applied chops which were different from those used by PAB and HXB.³⁵

(4) The completed bank confirmation forms were sent to Deloitte's audit department, which relied on them as evidence confirming the existence of the bank balances of the 5 Bank Accounts during the audit of the 2012 AFS and 2013 AFS³⁶.

51. Fourth, during cross-examination, Mr Wen admitted that the Falsification Scheme and the Fabrication Scheme had been perpetrated on the Group.

³⁴ Petition §53.

³⁵ Petition §§55-58.

³⁶ Petition §56.

52. The above evidence is sufficient to prove that the Company had used the Schemes to inflate the bank balances of the Group as stated in the 2012 AFS and 2013 AFS.

53. Nevertheless, the SFC said that according to its investigation:

- (1) In the Company's Records, there were numerous transactions described as "project funds" and "account transfers" and the credit and debit entries in the ledgers of the 5 Bank Accounts for the years 2012 and 2013 but no corresponding transactions could be found in CSRC's Records (collectively "**Fictitious Transactions**"). Details of the Fictitious Transactions are as follows:

	2012		2013	
	No.	RMB	No.	RMB
Debit entries/ transactions	327	(61,500,758)	708	(745,671,451)
Credit entries/ transactions	215	641,231,137	303	1,289,994,499
Net credit		579,730,379		544,323,048
Increase in cash & bank balance as stated in AFS		837,651,000		621,470,000
Net credit / Increase in cash & bank balance		69%		87%

- (2) The net credit created by the Fictitious Transactions represented 69% and 87% of the Group's net increases in bank / cash balances recorded in the 2012 AFS and 2013 AFS.

54. Although Ms Liao criticised the lack of particularity in respect of the Fictitious Transactions, she did not challenge any part of the

evidence of Mr Cheng where he referred to the relevant parts of ROIs and documents in support of the allegations. In my view, the criticism is misplaced. The Fictitious Transactions only go to illustrate *how* the Group recorded the fictitious bank balances (i.e. 2012 Discrepancy and 2013 Discrepancy) in the books of accounts of the Subsidiaries (without which the relevant accounting ledgers would not be balanced) and reinforces the fact that the Schemes were perpetrated on the Group. The SFC does not have to prove the precise manner in which the Group recorded the 2012 Discrepancy and 2013 Discrepancy.

55. For the above reasons, I find that the Schemes were devised and perpetrated on the 5 Bank Accounts. As a result of the Schemes, the bank balances of the Group stated in the 2012 AFS and 2013 AFS had been inflated by RMB 2.18 billion (i.e. 2012 Discrepancy) and RMB 2.72 billion (2013 Discrepancy) respectively.

D2. 2nd Issue: whether Mr Wen caused, directed and/or orchestrated the Schemes

56. Mr Wen denied that he had any knowledge of or involvement in the Schemes. In particular:

- (1) Although he was Chairman and ED of the Group, he left the day-to-day management and operation of the Group including the Subsidiaries to R3, R4 and R5. He relied entirely on R4.
- (2) The Finance Department was in charge of the bank accounts of the Subsidiaries. It dealt with the employees of PAB and HXB and provided the Company's Records to Deloitte during

the audit. The Finance Department reported to R5 who, in turn, reported to R4.

- (3) Mr Wen did not have access to or personal knowledge of the Group's bank accounts and had no reason to question the veracity of the bank statements of the 8 Bank Accounts.

57. In my judgment, Mr Wen plainly had knowledge of and was involved in causing, directing and orchestrating the Schemes for the reasons stated below.

58. First, it is not in dispute that the Subsidiaries were corporate vehicles used by the Company to secure water treatment projects in the Mainland and were at all times managed by *inter alios* Mr Wen:

- (1) According to the answer provided by SWC (on behalf of the Company) to the SFC on 2 May 2017, the Subsidiaries were "merely corporate vehicles to secure water treatment projects in the PRC, and were managed by the relevant staff of the Company and/or its subsidiaries. As such, there are no senior managerial staff specifically for the 3 Subsidiaries"

- (2) Since 7 November 2005 and at all material times, Mr Wen had been Chairman and ED of the Company.

- (3) Mr Wen was a director of the Subsidiaries at all material times.

- (4) Mr Wen was at all material times the legal representative of BJ Epure and BJ Sound. He signed at least 9 contracts on behalf of BJ Sound and BJ Epure.

59. Second, the undisputed evidence showed that Mr Wen had actual control of, and had full access to, the 5 Bank Accounts:

- (1) He was an authorised signatory of the 5 Bank Accounts.
- (2) In the account opening documents submitted by BJ Epure and BJ Sound to PAB and HXB, Mr Wen was listed as the responsible person of BJ Epure and BJ Sound. No other person was listed as authorised signatory of the accounts of BJ Epure at HXB (483), BJ Sound at HXB (551), BJ Sound at PAB (002) and BJ Epure at PAB (501).
- (3) As Mr Wen admitted under cross-examination, he had power to access the information and obtain documents from PAB and HXB in respect of the 5 Bank Accounts if he wanted.

60. Third, the undisputed evidence shows that all payments made by the companies within the Group had to be approved by Mr Wen and he made all decisions for the Company in that:

- (1) According to the Company's Financial System – Funds Management (“**Management System**”), all payments in respect of the works of the projects abroad should be directed to the Company, and the department concerned should prepare application for payment which had to be approved by the heads of the Finance Department, the Works Department and so on. It was only *after* the Chairman (Mr Wen) had signed the applications that payments could be paid by the Company. Mr Wen confirmed that the Management System accurately reflected the position at the time and he continued

to grant and sign such financial approvals until April 2015³⁷;
and

(2) According to the Management System, all transfers and payments to third parties of over RMB2 million for construction and RMB0.5 million for equipment, the approval of Chairman was required. Mr Wen confirmed that such requirement applied in 2013.³⁸

(3) Mr Yu confirmed that he reported to Mr Wen. Although R4 was CEO, in fact, the Company was being run by Mr Wen who made all the decisions, be that minor or major decisions.

(4) Mr Seow also confirmed that Mr Wen was the person in charge of the whole Company and its direction.

61. Fourth, Mr Wen's assertion that he was not involved in the day-to-day operation and financial matters of the Company and the Group and the same had been delegated to R3, R4 and R5 cannot be true in view of the following uncontradicted evidence:

(1) Mr Wen made all the decisions for the Group and was intimately involved in approving all the transfers and payments for the companies within the Group at the relevant times (see §§58-60 above).

(2) R3 was absent from the Group between 2010 and 2013.³⁹

³⁷ Mr Wen's ROI Q7.

³⁸ Mr Wen's ROI Q8.

³⁹ PKF report §3.3.14; admitted by Mr Wen [Day 2 (am), XX].

(3) For a great portion of time between 2011 and 2013, R4 was based in Saudi Arabia for work.⁴⁰

(4) R5 reported to Mr Wen.⁴¹

62. Fifth, as the person having actual control of the Subsidiaries and the 5 Bank Accounts, Mr Wen must knew that the Subsidiaries did not have bank balances of over RMB 2 billion (as stated in the 2012 AFS and 2013 AFS). This is reinforced by the fact that at all material times: (1) the Subsidiaries were principal subsidiaries of the Company and held the most significant assets of the Group according to the 2012 AFS and 2013 AFS; (2) Mr Wen was familiar with the financial position of the Group and of the Subsidiaries; and (3) Mr Wen was the only person who could approve payments of any significant amounts by the Subsidiaries.

63. Sixth, the Schemes were not one-off or insignificant incident but involved elaborate and coordinated actions taken over 2 years. These included (1) creating fictitious substantial bank balances by fabricating bank statements in respect of the 5 Bank Accounts; (2) creating fictitious transactions which resulted in payments of monies to and from the Subsidiaries (eg. the Fictitious Transactions); and (3) creating false credit and debit entries in the books of accounts of the Subsidiaries and of the Company. Such Schemes could only have been directed and orchestrated by the person with the highest authority in the Group who (i) was familiar with the financial position of the Subsidiaries, (ii) had the power to approve any project carried on by and payment to the Subsidiaries, (iii) had the

⁴⁰ Mr Yu's ROI. Mr Wen initially admitted this, but later retracted and said R4 only went to Saudi Arabia when problems arose [Day 2 (am), XX].

⁴¹ Mr Yu's ROI Q300-301, 331-340. Mr Wen initially conceded that he had called R5 to inquire into the Group's financials [Day 2 (am), XX of Mr Wen], but he later retracted and said he never had and did not call R5's mobile [Day 3 (am), XX of Mr Wen].

power to operate the 5 Bank Accounts and obtain any information and statements of such Accounts, and (iv) had unrestricted access to the books of accounts of the Subsidiaries. It is indisputable that Mr Wen was the *only* person in the Group who had the powers and the means to direct these coordinated actions. Although during cross-examination, Mr Wen asserted that certain unspecified employees in the Finance Department might had access to and used his personal chop in dealing with the 5 Bank Accounts, I do not accept his assertion which never featured in Wen 1st and makes no sense. Mr Wen did not proffer any explanation as to why he allowed the employees to have access to his personal chop.

64. Seventh, the Discrepancies were not very sophisticated or difficult to detect given that Emerson (a group of independent research analysts) was able to identify the existence of possible fictitious bank balances and revenues by analysing the business of the Group and the published financial statements of the Company in the past including the 2012 AFS and 2013 AFS. It is inconceivable that Mr Wen, who made all decisions for the Group and was familiar with its financial position, would not have been alerted to the existence of the massive Discrepancies.

65. Eighth, the manner in which Mr Wen dealt with the allegations in the Emerson Reports and the subsequent investigation carried on by the SFC is inconsistent with Mr Wen having no knowledge of or involvement in the Schemes as he alleged:

- (1) In February 2015, the Emerson Reports were published which contained very serious allegations against the Company, including (a) the Group's real cash/bank balances only averaged one third of the amounts disclosed, (b) the real

profitability was slightly over a quarter of what was disclosed, and (c) concerns about its inability to make social security payment in 2011.

(2) In response, the Company issued 3 clarification announcements in February 2015, under Mr Wen's name as Chairman, denying all allegations in Emerson Reports. At trial, Mr Wen tried to disown the clarification announcements and claimed that he simply approved their publication. I do not accept his evidence. If Mr Wen were unaware of the Schemes as he claimed, he would have caused the Company to take immediate and serious steps to investigate the allegations in particular the discrepancies in bank balances, rather than giving elaborate reasons to refute all the allegations in the Emerson Reports.

(3) Even after the discovery of the 2015 Cash Discrepancy, which suggested that one of the allegations in the Emerson Reports was well founded, followed by Deloitte's demand that the Company should take immediate steps to obtain bank statements from the banks, Mr Wen still failed to take any step to ensure that genuine statements were obtained from PAB and HXB. His attempt to shift the responsibility to the audit committee is unacceptable, as it was Mr Wen (not the audit committee) who had actual control of the Subsidiaries and the 5 Bank Accounts.

(4) Even by the time of the board meeting on 26 March 2015 when R4 claimed to have obtained banks statements from PAB and HXB, Mr Wen still did not ask for copies of the same

or take reasonable steps to verify or supervise and ensure investigation was done properly. His evidence was that he did not even see or ask to have a look at the bank statements.

- (5) It was Mr Wen's evidence that when the Company's Records were supplied to the SFC on 13 July 2015 and 4 August 2015, he had only looked at the cover letters but not the Company's Records. This was despite the fact that the s.183 Notice was addressed to him personally.

66. Had Mr Wen been unaware of the Schemes, he would have been very concerned about the allegations in Emerson Reports and would have been keen to cause the Company to carry out extensive and thorough investigations into the allegations. This is because the allegations, if true, would mean that the Company and his 50% shareholding worth a lot less than the shareholders' equity as stated in the 2012 AFS and the 2013 AFS.

67. Instead, Mr Wen did the complete opposite. He allowed all relevant personnel and documents relating to the 5 Bank Accounts to disappear after the SFC had issued the s.183 Notice in March 2015 in that:

- (1) All senior employees involved in the fictitious bank balances left the Company: R4 left on 18 December 2015, R5 left on 16 April 2016 (3 days after suspension of trading), R3 left in August 2016, and other relevant finance staff left in 2015-2016⁴². All of them left allegedly for personal reasons, without any record of any discussion or explanation on the

⁴² The relevant finance staff include (i) Si Zhi Qiang (司志強), who took part in the bank visit with Deloitte on 10 March 2015 and left employment on 25 July 2015; (ii) Zhang Xue (張雪), who left employment on 25 September 2016; and (iii) Zhang Yijie (張宜潔), who left employment on 17 February 2016.

Schemes and without leaving any contact details to the Company. It is implausible that Mr Wen would allow all senior employees to leave without even asking them to provide information and documents relating to the 8 Bank Accounts which the SFC had been investigating since at least mid-July 2015.

(2) The 5 Bank Accounts were cancelled and closed on 21 August and 2 September 2015, after BCP had provided the Company's Records to the SFC on 13 July 2015 and 4 August 2015. Mr Wen's assertion that he did not know or approve the closure of the 5 Bank Accounts is incredible, given that (as I so find) he had actual control of and access to the 5 Bank Accounts.

(3) All company chops of the Subsidiaries were changed. Mr Wen asserted that the change had been made without his knowledge or approval, and there was no record or explanation in respect of (a) the time of change, (b) the reason of replacement, and (c) the whereabouts of the original chops. The assertion cannot be true as Mr Wen was the person who made all the decisions for the Group and he was the legal representative of BJ Epure and BJ Sound. Without his approval qua legal representative, it was impossible for BJ Epure and BJ Sound to replace their chops.

(4) All financial records and bank documents of the Subsidiaries were allegedly lost in a fire on 25 November 2016. There was no credible explanation as to why the fire had only been reported to the local fire service on 30 December 2016. In

any event, the one-page report only described the named vehicle caught fire. It did *not* say that the vehicle was in any way related to the Group, still less that the vehicle carried all the records and bank statements of the Subsidiaries and the same had been destroyed in the fire. Nor was there any credible explanation as to why the incident had only been announced by the Company 7 months later, on 19 June 2017 or why the Company claimed that “some of the financial documents of the Company” were lost and/or damaged.

68. It was only after the disappearance of the relevant personnel and documents that in 2017, Mr Wen belatedly caused the Company to engage Gaowen Law Firm⁴³ and PKF to investigate the Discrepancies. As all the relevant personnel and documents had not been made available to them, they were only able to produce heavily qualified reports based on the Company’s information without any independent verification.⁴⁴

69. The timing and the surreptitious manner in which Mr Wen allowed the personnel and documents to disappear is consistent with and reinforces the SFC’s case that Mr Wen knowingly caused, directed and orchestrated the Schemes.

70. Lastly, taking into account the following facts (which are either not in dispute or are established by cogent evidence discussed above),

⁴³ Gaowen Law Firm’s report dated 25 December 2017, Mr Wen accepted that they were engaged in or around December 2017, they only tried to contact previous finance staff on 19 December 2017, and tried to contact the banks on the same day.

⁴⁴ PKF was purportedly engaged in January 2017, but its report was dated 8 January 2018. PKF’s report was compiled based on information provided by the Group only and they could not obtain *any* information in respect of the bank balances discrepancies.

the only inference which can be drawn is that the Schemes must have been carried out with the knowledge and approval of Mr Wen:

(1) The Management System and the way in which the Group had been managed show that Mr Wen's approval was required for all decisions made by the Group, and all payments and transfers of funds by the Subsidiaries could only be made *after* Mr Wen had signed the relevant applications for approval.

(2) The complexity of the Schemes, which involved creating substantial fictitious bank balances and the corresponding fictitious transactions and entries in the accounts of the Subsidiaries and of the Group over a prolonged period of time, required the participation of many senior employees including at least R4 and R5. Mr Wen was the only person who had the authority to direct and mobilise all these senior employees to engage in the fraud for the entire period.

(3) The fictitious bank balances of the 5 Bank Accounts were very significant to the Group in that:

(a) The balances in the 5 Bank Accounts represented 75% and 77% of the Group's bank balances and 84% and 91% of the Group's net assets as at 31 December 2012 and 31 December 2013 respectively.

(b) Mr Wen acknowledged that the Subsidiaries were important subsidiaries of the Group and contributed a substantial part of its assets and financial performance.

(4) Mr Wen admitted that he was familiar with the Group and the Subsidiaries. Other than bare denial, he has not proffered any explanation as to how he could have overlooked the fact that the balances of the 5 Bank Accounts and the net assets of the Group had been overstated by over RMB 2 billion.

(5) Mr Wen stood to gain the most financially from the Schemes. Amongst the senior management, he was the only one who held over 50% shareholding in the Company, whereas the other EDs (including R3 and R4) or senior officers (including R5) only held immaterial shareholding. Indeed, under cross-examination, Mr Wen accepted that if the share price of the Company increased, the value of his shareholding would also increase.

71. For the reasons explained above, there is compelling evidence to prove that Mr Wen knowingly caused, directed and orchestrated the Falsification Scheme and the Fabrication Scheme.

D3. 3rd Issue: whether Mr Wen took a blind eye to the Schemes

72. The SFC puts this as an alternative case against Mr Wen, presumably on the assumption that taking a “blind eye” to the Schemes is not or cannot be equated with dishonesty. The assumption goes against the authorities where the courts explained that a person deliberately closing one’s eyes and ears and not asking questions of the fraud to avoid confirmation of the facts in whose existence there is a good reason to believe is as dishonest as a person having actual knowledge (see *Royal Brunei Airlines v Tan* [1995] 2 AC 378, at 389-391, per Lord Nicholls;

Grupo Torras v Al-Sabah [2001] LI Rep PN 117; *Twinsectra Ltd v Yardley & ors* [2002] AC 164, at 195, per Lord Millett; *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd* [2003] 1 AC 469, at §116, per Lord Scott; *Barlow Clowes International Ltd (in liquidation) v Eurotrust International Ltd* [2006] 1 All ER 333, §§10-12, per Lord Hoffmann).

73. In light of the findings under section D2 above, it is unnecessary to consider whether Mr Wen took a blind eye to the Schemes.

D4. 4th Issue: whether Mr Wen acted negligently in allowing the Schemes to be perpetrated

74. This is the other alternative case made by the SFC against Mr Wen.

75. If, contrary to the above findings, Mr Wen had no knowledge or involvement in the Schemes, it is necessary to consider whether he acted in breach of his duty to exercise proper skill, care and diligence as an ED of the Company.

76. Although Mr Wen made no admission on the breach of duty of care, skill and diligence as alleged in the Petition, it is clear from his oral evidence that he did *not* take issue with the SFC's case on negligence as pleaded in the Petition⁴⁵. This is reinforced by the fact that Ms Liao did not make any submissions in respect of the SFC's case on negligence.

77. The principles are not in dispute. As Mr Suen submitted:

⁴⁵ Petition §§84-88.

- (1) A director owes a duty to exercise such care, skill and diligence as would be exercised by a reasonably diligent person with the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions of a director in relation to the company and the general knowledge, skill and experience that the director has.⁴⁶ Such duty can be found in common law (*Re Long Success International (Holdings) Ltd*, §31, per Coleman J; *Re D'Jan of London Ltd* [1993] BCC 646 at 648 per Hoffmann LJ (as he then was), s.465 of the Companies Ordinance (Cap. 622) and the Listing Rules r.3.08(f)⁴⁷).
- (2) A director is under a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business and affairs to enable them to properly discharge their duties as directors. Whilst a director is entitled to delegate particular functions to others, he remains under a duty to supervise the discharge of the delegated functions (*Re Copyright Ltd* [2004] 2 HKLRD 113, §§34-35; *Re Long Success*, §33).
- (3) The duty incorporates a duty to supervise the affairs of the company's subsidiaries (*Re Long Success*, §32).
- (4) A director must read and understand the financial statements of the company and consider whether they are consistent with his knowledge of the company's financial position and statutory requirements, and make enquiries if matters revealed

⁴⁶ Petition §§60-61.

⁴⁷ For which the Company and each of the director gave an undertaking to the SEHK to comply with.

in the financial statements call for such enquiries. (*Law of Companies in Hong Kong*, 3rd ed., §8.158).

78. As stated in the 2012 Annual Report of the Company, and was not in dispute:

(1) Mr Wen had responsibility for the overall management and corporate governance of the Group, and had a duty to ensure that the business of the Group was effectively managed and properly conducted day-to-day; and

(2) Mr Wen had direct responsibility in considering and approving the financial results of the Group, overseeing its business and affairs; reviewing and approving material acquisitions and disposal of assets; reviewing a framework for proper internal controls and risk management; and ensuring the Group's compliance with laws, regulations, policies, guidelines.

79. In view of the duty of care and skill owed to the Company and his responsibility in the Group, Mr Wen ought to have:

(1) a proper understanding and knowledge on the overall business, finances and performance of the Group including its bank balances;

(2) taken steps to ascertain and satisfy himself that the financial position including the bank balances reported in the 2012 AFS and 2013 AFS were accurate or within a reasonable range;

- (3) procured the Group to provide the regulators (SFC and SEHK) and the investing public with all material information and documents, and to ensure that such information and documents were complete and true.

80. If, contrary to my findings in section D2 above, Mr Wen did not knowingly caused, directed and orchestrated the Schemes, on Mr Wen's own evidence, he failed to do any of the above acts. This was despite the allegations raised in the Emerson Reports in February 2015, followed by the concerns raised by Deloitte on 12 March 2015 and the investigation undertaken by the SFC from 16 March 2015. A reasonable person standing in the position of Mr Wen would have asked questions and made all necessary enquiries to ensure that the amounts of bank balances stated in the 2012 AFS and 2013 AFS were accurate, and would have caused the Company to carry on extensive and thorough investigations into all the concerns raised so as to ensure that the financial position of the Group had not been overstated. None of these steps were undertaken by Mr Wen despite the fact that he remained Chairman and ED of the Company throughout the period.

D5. 5th Issue: whether Mr Wen gave false or misleading explanations regarding the 2015 Cash Discrepancy

81. It is not in dispute that following Deloitte's discovery of the 2015 Cash Discrepancy in March 2015, Mr Wen provided the 1st Explanation and 2nd Explanation to the board and the audit committee in that:

(1) At the meetings of 11 and 12 March 2015, Mr Wen proffered the 1st Explanation, admitting that he had used RMB 2 billion cash belonging to the Group for *his* other business.

(2) However, at the board meeting on 19 March 2015, Mr Wen proffered the 2nd Explanation which suggested that RMB 2 billion cash had been used for the Proposed Acquisitions for the Group.

82. As it is Mr Wen's case that the 2nd Explanation represented the true position, the 1st Explanation must be false. Ms Liao has not advanced any explanation as to why Mr Wen provided such false information to the board and the audit committee.

83. As regards the 2nd Explanation, the evidence before the court shows that the 2nd Explanation must be false.⁴⁸

84. First, there was no dispute that the Group's bank balances in the 2012 AFS and 2013 AFS had been overstated by RMB 2.18 billion and RMB 2.72 billion respectively. If one deducts the 2012 Discrepancy and the 2013 Discrepancy from the Group's "bank balances and cash" in the 2012 AFS and 2013 AFS, the Group only had "bank balances and cash" of RMB 732 million and RMB 814 million as at 31 December 2012 and 2013 respectively. This means that the Group would not have RMB 2 billion cash alleged to have been withdrawn from its bank accounts in November 2014.

⁴⁸ Petition §§77, 78(3).

85. Second, the CSRC's Records show that none of the 3 alleged payments of (1) RMB 600 million on 4 November 2014, (2) RMB 870 million on 24 November 2014, and (3) RMB 530 million on 24 November 2014, referred to by Mr Wen and formed part of his 2nd Explanation, had in fact been paid out of the 8 Bank Accounts.

86. Third, although Mr Wen asserted that RMB 2 billion had been paid as earnest money for the Proposed Acquisitions, he has not produced any documents in respect of the Proposed Acquisitions.

87. The 2nd Explanation was admittedly provided by Mr Wen to, and relied upon by RSM and PKF, which were engaged by the Company to investigate the 2015 Cash Discrepancy. The conclusions of the reports of RSM and PKF were announced by the Company to the members and provided to SEHK and the SFC⁴⁹.

88. In her Closing, Ms Liao submitted that "there is no evidence to suggest that the Proposed Acquisitions are not genuine" and reliance was placed on RSM's conclusions which she said had been reached by RSM after carrying out on-site inspections of the projects, conducting extensive interviews and forensic analysis of the Company's staff and electronic documents relating to the Proposed Acquisitions. The submission misses the point. The burden is on Mr Wen to prove his assertions (i.e. that the Proposed Acquisitions were genuine and RMB 2 billion was paid by the Group for such Acquisitions). It is not for the SFC to prove a negative. As for RSM's conclusions, they were based on the 2nd Explanation provided

⁴⁹ RSM's report dated 20 November 2015 and the announcements dated 31 August 2015 and 18 December 2015. PKF's report dated 9 June 2015 and the announcement dated 23 June 2015.

by Mr Wen. The conclusions cannot be right in view of the facts and matters stated in §§84 - 86 above.

89. Lastly, Ms Liao argued that it was reasonable for Mr Wen to form the view that the Company as a whole had sufficient funds to pay for the earnest money. Reliance was placed on the 2013 AFS which referred to the funds raised by the Company in 2013 and Mr Yu's evidence where he said that his impression was that the Company had sufficient funds at its disposal in 2012-2013. The argument is flawed. The issue is whether the 1st and 2nd Explanations were false. For the reasons stated, the Group could not have the cash/bank balances to pay the earnest money and none of the 3 alleged payments were in fact paid out of the 8 Bank Accounts. It is irrelevant whether Mr Wen thought that the Company had sufficient funds to pay the earnest money.

90. For the above reasons, there is cogent evidence in support of the SFC's case that Mr Wen gave false explanations regarding the 2015 Cash Discrepancy to the other members of the board, the audit committee, Deloitte, RSM, PKF, the members of the Company and the regulators (i.e. SEHK and the SFC).

D6. 6th Issue: whether the business and affairs of the Company were conducted in an unfairly prejudicial manner

91. The principles are not in dispute.

92. The SFC has to satisfy the 3 conditions stipulated in s.214 of the SFO namely, (1) the corporation in question is or was a listed corporation; (2) the business or affairs complained of is that of the

corporation; and (3) the conduct complained of falls within one or more heads of misconduct specified in s.214(1)(a)-(d).

93. As regards the second condition, the conduct complained of can be that of the listed company and the subsidiaries directed by or under the control of such listed company (*Re Shandong Molong Petroleum Machinery Company Limited* [2021] HKCFI 497, §17).

94. Section 214(b), (c) and (d) of the SFO prescribes the various heads of misconduct and may be summarised as follows.

95. With respect of s.214(1)(b):

(1) “Misfeasance” is defined in Part 1 of Schedule 1 to the SFO as “the performance of an otherwise lawful act in a wrongful manner”. The notion of “misfeasance” overlaps with that of breach of fiduciary duty and seemingly covers a wide range of conduct (*SFC v Yeung Chung Lung*, HCMP 205/2013, 17 February 2017, §81).

(2) The words “other misconduct” connote improper or wrong behaviour or mismanagement, or culpable neglect of duties. This term is something of a “belt and braces exercise”, and is intended to cover the “widest range of possible misconduct” (*Re DBA Telecommunication (Asia) Holdings Limited* [2022] HKCFI 653, §10; *Re Long Success*, §37).

(3) A breach of the duty to exercise reasonable care and diligence in the management of company may constitute both

“misfeasance” and “other misconduct” (*Re DBA Telecommunication*, §10; *Re Long Success*, §37).

96. As for s.214(1)(c) (i.e. members not having been given all the information with respect to its business or affairs that they might reasonably expect), it can be complementary to the other subsections (*SFC v Yeung Chung Lung*, HCMP 205/2013, 17 February 2017, §84; *Re Long Success* §38), and covers situations such as (1) the making of misleading or false announcements; and (2) situations requiring publication of periodic financial statements and announcements, as members are entitled to expect the listed company to provide complete and accurate information in respect of such matters (*SFC v Li Wo Hing*, HCMP 1023/2011, 26 September 2012, §§10(1)(b), 10(2)(a); *Re Shandong Molong*, §19(2)).

97. With respect to s.214(1)(d):

(1) The conduct in question does not have to be wrongful *per se* (*Re Shandong Molong*, §19(3)).

(2) “Unfairly prejudicial” conduct covers a range of conduct, from fraud at the one end to neglect or inaction on the part of those to whom the affairs of a company are entrusted on the other end. The question to be asked in such circumstances is whether the conduct concerned is that which can be expected from the managers of the company to whom those affairs have been entrusted (*SFC v Fung Chiu* §22; *Re Long Success* §39).

98. In the present case, all 3 conditions stipulated in s.214 of the SFO are satisfied.

99. It is not in dispute that the first and second conditions are satisfied.

100. In view of the findings on the 1st Issue, the 2nd Issue and the 5th Issue, there is more than sufficient bases for the court to conclude that the business and affairs of the Company were conducted by Mr Wen in a manner within the meaning of s.214(1)(b), (c) and (d) of the SFO in that:

(1) The Schemes were fraud perpetrated on the Company and the Subsidiaries, which constituted misfeasance or misconduct within the meaning of s.214(1)(b) of the SFO;

(2) The provision of false explanations (i.e. the 1st and 2nd Explanations) on the 2015 Cash Discrepancy constituted misfeasance or misconduct under s.214(1)(b);

(3) The Schemes and the provision of false explanations resulted in the Company's members not having been given all the information with respect to the Company and the Subsidiaries' business and affairs that they might reasonably expect under s.214(1)(c) of the SFO;

(4) The Schemes and the provision of false explanations were unfairly prejudicial to the Company and its members under s.214(1)(d) in that the financial position of the Group had been grossly overstated and the true position remains unknown. The Company and its members (other than Mr Wen and his companies) were prejudiced as trading of the Company's shares had since April 2016 been suspended, and there was no indication as to whether trading would resume, if at all.

D7. 7th Issue: Remedies

101. It is not in dispute that if the court is of the opinion that the business or affairs of the Company have been conducted in the manner described in s.214(1), the court may make any order stipulated in s.214(2) including a disqualification order against the person responsible for the impugned conduct if it considers it justified (*Re Long Success* §40).

D7.1 Disqualification order

102. The principles governing the exercise of discretion in making a disqualification order may be summarised as follows:

(1) The court takes into account the two-fold objectives of a disqualification order viz., to protect the public against the future conduct of the respondent and as a general deterrence (*Re Shandong Molong* §20).

(2) The court will have regard to a wide spectrum of factors, including the respondent's age and state of health, the length of time he has been in jeopardy, whether he has admitted the offence, his general conduct before and after the offence, and the periods of disqualification of his co-directors that may have been ordered (*Re First China Financial Network Holdings Ltd* [2015] 5 HKLRD 530 §8).

(3) There are 8 criteria which govern the court's exercise of discretion namely (a) the character of the offenders, (b) the nature of breaches, (c) the structure of the companies and the nature of their business, (d) the interests of the shareholders, creditors and employees, (e) the risks to others from the

continuation of the offenders as company directors, (f) the honesty and competence of the offenders, (g) the hardship to the offenders and their personal and commercial interests, and (h) the offenders' appreciation that future breaches should result in future proceedings (*Re First China Financial Network* §8; *Re DBA Telecommunication* §31(4)).

(4) The court adopts a reasonably broad-brush approach, and will have regard to 3 brackets of disqualification periods:

- (a) the top bracket of disqualification for over 10 years for particularly serious cases;
- (b) a minimum bracket of below 5 years' disqualification for cases which are relatively less serious; and
- (c) a middle bracket of 6 to 10 years' disqualification for cases which although serious, are not so serious as to merit a period of disqualification in the top bracket (*Re First China Financial Network* §§5-6, 9; *Re DBA Telecommunication* §§31(2)-(3)).

103. Mr Suen submitted that a disqualification period of 10 to 11 years is appropriate to reflect the gravity of the misconduct, the deliberate and misleading explanations proffered, and the need for deterrence and protection of the investing public against Mr Wen's wrongdoing. The court in *Re Shandong Molong* adopted a starting point of 11 years for the 2nd respondent, who was Chairman and ED of the company, and the misconduct did not involve embezzlement of funds or loss suffered by the company (§§29-30).

104. Ms Liao on the other hand emphasised that the Company had not suffered any loss, and Mr Wen's conduct was less serious than the conduct of the 1st respondent in *SFC v Li Hejun*, HCMP 166/2017, 4 September 2017. I disagree. The 1st respondent in *SFC v Li Hejun* acted in breach of his fiduciary duty in failing to cause the company to collect a very substantial amount of receivables owed by entities under his control. His conduct fell within the top end of the middle bracket as it did not involve any fraud or mis-statement of the financial position of the company.

105. I consider that a disqualification period of 12 years is appropriate given the very serious nature of the misconduct, which involved fraud and dishonesty on the part of Mr Wen, who is found to have caused, directed and perpetrated the Falsification Scheme and the Fabrication Scheme for over 2 years. He also provided false explanations on the 2015 Cash Discrepancy to the audit committee, auditors, members and the regulators. Such conduct was highly prejudicial to the Company and its members and resulted in suspension in trading for a prolonged period substantial time and costs were incurred by the Company to engage various entities to investigate the impugned transactions as required by the audit committee and the regulators. Worse still, after the SFC had taken step to investigate the affairs of the Company, Mr Wen caused or allowed all relevant personnel and documents to become unavailable. This made it impossible for the SFC and the Company to conduct a thorough investigation into the Schemes and the 2015 Cash Discrepancy, which is necessary to identify the full extent of the prejudice or damage suffered by the Company and to take steps to address and rectify the same.

D7.2 Share purchase order

106. The SFC seeks an order requiring Mr Wen do make an offer to purchase the shares held by other members at a price to be determined by the court.

107. Section 214(2)(e) of the SFO provides that the court may “make any other order it considers appropriate, whether for regulating the conduct of the business or affairs of the corporation in future, or for the purchase of the shares of any members of the corporation by other members of the corporation or by the corporation.... or otherwise”. The share purchase order sought by the SFC falls within the ambit of s.214(2)(e). There is no dispute that Mr Wen is a member of the Company.

108. Contrary to Ms Liao’s contention⁵⁰, the grant of a purchase order does not require the SFC to establish that there was any financial gain received by the respondent or any loss suffered by the company/members. Nor does it require the SFC to prove that such gain / loss was quantifiable and was caused by the misconduct:

- (1) There is no such requirement in s.214(2)(e).
- (2) The authorities relied on by Ms Liao (*Re Styland Holdings Ltd (No 2)* [2012] 2 HKLRD 325, §§106, 139, 142; *SFC v Wong Wai Kwong David* [2021] HKCA 897, §§36-39; *SFC v Yeung Chung Lung*, HCMP 205/2013, 17 February 2017, §§94, 109; *SFC v Li Wo Hing*, HCMP 1023/2011, 26 September 2012, §§8, 10, 18(3)) are distinguishable. In all these cases, the court had to consider whether to make an order requiring the

⁵⁰ Opening §§16, 18 &19

respondent to *compensate* the company for the loss suffered. It was in that context that the court had to consider whether the evidence established (a) some financial advantage was received by the respondent or financial loss was caused to the company; (b) the financial advantage / loss was readily quantifiable; and (c) the causal link between the conduct and the financial advantage / loss.

- (3) Where, as here, the order sought is a share purchase order, no such consideration arises as the court does not have to be concerned about whether the compensation ordered to be paid by the respondent would result in a windfall or double recovery to the company.

109. In considering whether a share purchase order should be made against a respondent, the court may be guided by the principles applicable to an “unfair prejudice” petition under ss.724-725 of the Companies Ordinance (Cap. 622) (“CO”) (which replaced s.168A of the former Companies Ordinance (Cap. 32)), given the similarity in wordings and width of both provisions. As noted by Barma J (as he then was) in *Re Styland Holdings (No 2)*, §138, both provisions are designed to provide the court with a high degree of flexibility in terms of the remedies it might provide.

110. In my view, the court should take into account the following differences between the 2 statutory remedies in that under s.214(2)(e):

- (1) The petitioner is the SFC, which pursues the proceedings in the interests and for the benefit of the company and its members, and to redress wrongful conduct of those concerned

in the management of listed company for the protection of the public. By contrast, the petitioner under ss.724-725 of the CO pursues the proceedings to advance his private interest and generally, public interest does not come into play.

(2) The company in question is a listed company. Its constitution contains no restriction on transfer of shares, and the members are at free to buy and sell their shares through the SEHK or by private agreement. This means that if members are dissatisfied with the manner in which the affairs of the company has been conducted, they can extricate the investment by selling their shares through the market without any impediment.

(3) Generally, there is greater transparency in the manner in which the business and affairs of the listed company have been conducted as the board has to make disclosure and announcement to the members in accordance with the requirements of the Listing Rules. In this sense, it may be said that if the company had made announcements on matters relating to the misconduct, their impact would have been reflected (at least in part) in the prices of the shares of the company. For those investors who decided to acquire shares in the company with the knowledge of the matters disclosed or announced by the board, they voluntarily assumed the risk that they may not be able to sell their shares if the regulators decide to suspend trading of the shares.

111. In view of the aforesaid differences, in deciding whether to make a share purchase order in the context of a listed company, the court may take into account the following factors:

- (1) whether there is a lesser remedy sufficient to deal with the unfairly prejudicial conduct and there is no likelihood of the conduct repeating;
- (2) where there are difficulties or impracticalities in framing orders for regulating the company's affairs in future or to remedy the misconduct;
- (3) whether the other members would otherwise be locked in the company due to difficulties in disposing of the shares (cf. *Lo & Qu, Law of Companies in Hong Kong* §10.211; *Re Elgindata Ltd* [1991] BCLC 959 at 1005g-i);
- (4) whether the person against whom the order is sought was in control of the company at the material times of the misconduct and his interests in the company; whether he acted in clear disregard of the interests of the minority shareholders; his pattern of conduct and whether he acted in breach of the Listing Rules and other applicable regulations (*Re Mandarin Resources Corporation Limited*, HCCW 348/1996, 19 November 1999, pp.5-6, 103, 109-110, a case decided on the now repealed Securities and Futures Commission Ordinance (Cap. 24)); and
- (5) whether the respondent has the financial means to comply with the order. In this regard, I do not agree with Mr Suen's submission that the fact that the respondent is impecunious

may not be a sufficient ground to deny the petitioner a buy-out order where it is otherwise appropriate, citing *Lo & Qu, Law of Companies in Hong Kong* §10.211; *Re Cumana Ltd* [1986] BCLC 430 at 436h-437b. Generally, the court would not make an order in vain. It does not serve the interests of justice to order a respondent to purchase the shares of other members if the evidence shows that the respondent does not have the financial means to comply with such order.

112. Applying the above principles, I consider that it is an appropriate case where the court should make an order requiring Mr Wen to make an offer to purchase the shares held by other members (i.e. other than companies owned or controlled by Mr Wen). There are 4 reasons for this.

113. First, as a result of the Schemes and the 2015 Cash Discrepancy, the true financial state of the Company and of the Group remains unclear. The position is exacerbated by the subsequent disappearance of all relevant personnel and documents, which render it impossible for the SFC and the Company to identify the full extent of the wrongs done to the Group and whether any financial loss has been suffered by the Group. The latter also means that the Company would not be able to bring any proceedings and seek compensation against the persons responsible for causing the loss to the Company.

114. Second, the prejudice suffered by the Company and its members is substantial and irreversible in that:

- (1) The existence of the Discrepancies and the 2015 Cash Discrepancy and the inability of the Company to conduct full investigation and redress the same would inevitably affect the confidence of the financiers and investors who might otherwise be willing to advance loans to or invest in the bonds or shares issued by the Company as any seasoned financier and investor would require accurate and complete financial information before deciding to advance loans to or invest in the Company.
- (2) Trading in the Company's shares has been suspended for over 6 years. According to the announcement dated 1 August 2018, the SEHK imposed 2 resumption conditions on the Company namely: (1) publication of all outstanding financial results of the Group in accordance with the Listing Rules and address any audit modification; and (2) restoring and maintaining sufficient public float under rule 8.08(1)(a) of the Listing Rules. According to the announcement dated 4 December 2020, the SEHK added a 3rd resumption condition requiring the Company to demonstrate compliance with rule 13.24 of the Listing Rules.
- (3) To-date, there is no indication that the Company will be able to comply with the above conditions. If and for so long as trading remains suspended, the other members will not be able to sell their shares through the SEHK. It is no answer to say that these members may still sell their shares through private agreements as the members acquired their shares on the basis that the Company's shares could be traded on the SEHK.

(4) Further, trading of the shares has been suspended for more than 12 months as at 1 August 2018 and may be delisted under rule 6.01A(2)(b)(ii) of the Listing Rules. According to the announcement dated 8 February 2022, the SEHK after consultation with the SFC would withhold exercising its right to cancel the listing of the Company under rule 6.01A(2)(b)(ii) until 31 July 2022. These show that the SEHK may cancel the listing of the Company's shares at any time.

115. Third, there is no lesser remedy which may redress the Discrepancies and the 2015 Cash Discrepancy. In particular, the relief sought by the SFC against the Company, even if granted, would not redress the wrongs done to the Company. Indeed, the futility of the appointment is illustrated by the fact that the Company has previously engaged RSM, PKF and other law firms to investigate the Discrepancies and the 2015 Cash Discrepancy, and the heavily qualified reports produced by such firms.

116. Fourth, there is no suggestion that Mr Wen does not have the financial means to purchase the shares of the other members. Indeed, since June 2017, Mr Wen has indicated to the board that he intends to privatise the Company albeit that he has not taken any concrete steps to pursue such privatisation.

117. Ms Liao contended that based on the disclosure of interests as of 16 June 2022, the second largest shareholders holding 32.53% shares in the Company appear to be institutional investors. There is no evidence that the SFC has sought the view of such investors or indeed, any members. There is no evidence of any complaint from any members or that they

prefer a share purchase order. I do not think that these matters, even if correct, are relevant to the consideration as to whether a share purchase order should be made. The order sought by the SFC is that Mr Wen be ordered to make an *offer* to purchase the shares of the other members at the price to be determined by the court. It is a matter for the members to decide whether they want to accept the offer.

E. DISPOSITION AND COSTS

118. For the reasons set out above, I find that:

- (1) the Schemes were perpetrated on the 5 Bank Accounts. As a result of the Schemes, the bank balances of the Group stated in the 2012 AFS and 2013 AFS had been inflated by RMB 2.18 billion and RMB 2.72 billion respectively;
- (2) Mr Wen plainly had knowledge of and was involved in causing, directing and orchestrating the Schemes;
- (3) Mr Wen gave false explanations regarding the 2015 Cash Discrepancy to other members of the board, the audit committee, Deloitte, RSM, PKF, members of the Company and the regulators; and
- (4) the business and affairs of the Company were conducted by Mr Wen in a manner within the meaning of s.214(1)(b), (c) and (d) of the SFO.

119. As for relief, I make the following order against Mr Wen:

- (1) A disqualification order for 12 years from the date of this Judgment; and

- (2) An order that Mr Wen shall make an offer to purchase the shares held by the other members of the Company (i.e. members other than himself and the companies owned and/or controlled by him) at the price to be determined by the court at a further hearing.

120. For the above purpose, the SFC is directed to submit within 14 days of this Judgment (1) a draft setting out the proposed terms of the order; and (2) the proposed directions on the court's determination on the price at which Mr Wen shall make an offer to purchase the shares held by the other members, taking into account the comments which have been made by Mr Wen (if any). If the parties are unable to agree on the wordings, the SFC is to lodge the draft orders setting out the terms which are in agreement and those which the parties are not able to agree and the respective contentions of the parties.

121. As for costs, I make a costs order *nisi* that:

- (1) Mr Wen do pay the costs of and occasioned by the Petition including the costs of trial to the SFC on an indemnity basis, to be taxed if not agreed and with certificate for 2 counsel. The higher scale of costs reflects the gravity of the misconduct.
- (2) Mr Wen do pay the costs incurred by the Company in the Petition on an indemnity basis. This reflects the fact that the Company is only a nominal party and is the victim of the fraud committed by Mr Wen against it, and should be entitled to recover the costs occasioned by the Petition from Mr Wen.

122. The present case is a paradigm example where the directors of a listed company were able to avoid the enforcement action taken by the SFC by choosing to stay out of the jurisdiction. It is a matter well known to the regulators and practitioners that service of the originating process such as a petition on persons who stay in the Mainland often require many months and may even be futile when the persons deliberately took steps to avoid being served by the relevant authorities. The regulators in particular the SEHK may want to review the position and address the problem sooner than later. One possible avenue available to the regulators would be for the SEHK to require any person who assumes the position as director of a listed company to agree, as part of the undertaking he/she gives to the SEHK, to designate a place within the jurisdiction at which the regulators may serve the originating process on him/her when they take enforcement action against such director. There is no reason why a person who agreed to assume the important role as director of a listed company and to abide by the duties imposed by the Listing Rules and other relevant regulations would be able to avoid enforcement action by choosing to stay out of the jurisdiction.

(Linda Chan)
Judge of the Court of First Instance
High Court

Mr Jenkin Suen SC leading Ms Sheena Wong, instructed by Securities and Futures Commission, for the Petitioner

Mr Thomas WK Wong, instructed by Stevenson, Wong & Co., for the 1st Respondent (on 14 June 2022 only)

Ms Tara Liao, instructed by DLA Piper Hong Kong, for the 2nd Respondent