The report of the Market Misconduct Tribunal into dealings
in the shares of Evergrande Real Estate Group Limited
on 21 June 2012

**Part II: A report pursuant to section 252(3)(c) of the Securities and Futures Ordinance, Cap. 571**

## INDEX

# CHAPTER 8

# ORDERS

## *A. Background.*

257. In its report of 26 August 2016 ('the Report'), the Tribunal found that the single 'Specified Person', Mr Left, was culpable of market misconduct within the meaning of s.277 of Part XIII of the Ordinance. In accordance with the terms of that section, the Tribunal found –

(i) That in June 2012, Mr Left had published, that is, he had disseminated, a document under the name of 'The Citron Report', that document containing what was advertised as being research and analysis compiled over several months which concluded that Evergrande Real Estate Group Limited ('Evergrande'), a company listed on the Hong Kong Exchange, was essentially an insolvent company that had consistently presented fraudulent information as to its accounts to the investing public.

(ii) That certain of the information contained in that published document, namely, that Evergrande had been culpable of fraudulent accounting and that in reality it was insolvent, was likely to impact on the Hong Kong market in one or more of the ways set out in s.277(1).

(iii) That the information was false and/or misleading as to material facts or through the omission of material facts.

(iv) That, as its primary finding, Mr Left had been reckless as to whether such information was false and/or misleading as to material facts or through the omission of material facts.

(v) In finding that Mr Left had been reckless, the Tribunal found that, when he came to publish his report, first, Mr Left was aware of the risk that the information in it going to the assertions of fraudulent accounting and the fact that Evergrande was essentially insolvent were false and/or misleading; second, he was further aware that in the circumstances the risk was of such substance that it was unreasonable to ignore it; third, nevertheless, he went ahead and published.

258. On Wednesday, 19 October 2016, the Tribunal was convened again to consider the matter of consequential orders.

259. In this regard, the Tribunal was assisted by written submissions filed on behalf of the SFC by its leading counsel, Mr Peter Duncan SC. No written submissions on behalf of Mr Left were placed before the Tribunal although Mr Left's solicitor, Mr Francis Comtois[1], appeared at the hearing and was invited, if he so wished, to make appropriate representations. He informed the Tribunal that he had received no instructions to make representations.

[1] Of Timothy Loh LLP

260. Having heard from Mr Duncan, and after retiring to consider the appropriateness of the consequential orders to be made, the Tribunal reconvened to announce its orders, saying that a written decision would later be handed down.

*B. The orders imposed*

261. The orders made by the Tribunal, together with a brief description of their nature and purpose, were as follows –

S.*257(1)(b): 'the cold shoulder' order*

262. This section gives the power to the Tribunal to impose what are commonly called 'cold shoulder' orders. Unless the leave of the Court of First Instance is first obtained, a cold shoulder order has the effect of prohibiting a person who is the subject of the order from any dealings, direct or indirect, in the Hong Kong financial market for the life of the order. Failure to comply with such an order constitutes a criminal offence. If a person aids or abets the avoidance of a cold shoulder order that person commits an offence. Even though such an order may result in financial loss, it is settled that this effect is incidental and subservient to the primary intention of protecting the public. The order is designed, therefore, to safeguard our financial markets. The Ordinance provides that a cold shoulder order shall not be imposed for a period of time exceeding five years.

263. Having regard to the circumstances of Mr Left's culpability, the Tribunal determined that, as a protective measure, it was necessary to impose a cold shoulder order for the maximum period of five years calculated from the date of the order, that is, from 19 October 2016.

*S. 257(1)(c): cease and desist order*

264. This section gives the power to the Tribunal to order that the person identified as having engaged in market misconduct shall not again perpetrate any conduct which constitutes such market misconduct as is specified in the order. Such orders, known as 'cease and desist' orders, permit trading but, on pain of criminal punishment, seek to ensure that all future dealings by that person will not constitute market misconduct. Such orders are made in perpetuity. Our courts have held that 'cease and desist' orders are preventative, that is, protective and not penal.

265. Having regard to the circumstances of Mr Left's culpability, the Tribunal determined that, as a protective measure, it was necessary to impose a cease and desist order, the misconduct, however, being restricted to that form of misconduct identified in the present proceedings, namely, a finding of culpability pursuant to s.277(1), and no other form of misconduct.

*S.257(1)(d): disgorgement of profit*

266. This section empowers the Tribunal to order that a person found culpable of market misconduct pay to the Government "an amount not

exceeding the amount of any profit gained as a result of the market misconduct in question".

267. As a result of discussions between Mr Duncan and Mr Comtois, it was agreed that the amount to be disgorged should be HK$1,596,240 and an order in that amount was made.

268. In respect of interest, it was ordered that, pursuant to s.259 of the Ordinance, Mr Left pay to the Government compound interest on that sum calculated at one year rests from 21 June 2012 at the rate from time to time applicable to judgment debts under s.49 of the High Court Ordinance, Cap 4.

*S.257(1)(e) and (f): Costs*

269. These two sub-sections give to the Tribunal the power, in the exercise of its discretion, to order that a person shall pay to the Government such sum as it considers appropriate for the costs and expenses incurred by the Government and to order that a person shall pay to the Securities and Futures Commission ('the SFC') such sum as it considers appropriate for the costs and expenses incurred by the SFC.

270. In respect of costs orders, the Tribunal ordered as follows:

(i) That Mr Left do pay to the Government the sum of $1,259,179 being the costs and expenses reasonably incurred by the

Government in relation to or incidental to the Tribunal proceedings.

(ii) That Mr Left do pay to the SFC a total sum of HK$3,966,861 being HK$3,623,600 on account of the costs and expenses reasonably incurred by the SFC in relation or incidental to the Tribunal proceedings and a sum of HK$343,261 on account of the costs and expenses reasonably incurred by the SFC in relation or incidental to the investigation carried out before the Tribunal proceedings were instituted.

*S.264(1): registering orders with the Court of First Instance*

271. Pursuant to this section, the Tribunal ordered that written notice be given in order to register all relevant orders in the Court of First Instance.

*C. The Tribunal's reasons for imposing the 'cold shoulder' order and the 'cease and desist' order*

272. In imposing a cold shoulder order with a life of five years, the Tribunal recognised that it was imposing an order that would endure for the maximum period of time permitted by the statute. However, it was of the view that the relevant circumstances demanded the imposition of such an order and that it be imposed together with a cease and desist order of limited reach.

273. In coming to its decision, the Tribunal took a number of factors into account which are summarised as follows.

274. In the view of the Tribunal, it was important at the outset to take into account the protective nature of the cold shoulder order. In doing so, it was clear that the principal objective of the order is the protection of the integrity of the market, that is, the assurance that it remains fair and transparent. The Tribunal also took into account that the protective nature of a cold shoulder order is intended to protect all market participants, general investors included. In this regard, the Tribunal was prepared to accept that perhaps professionals in the market may have approached the attack on the integrity of Evergrande with a degree of cynicism, they may even have seen an opportunity to profit from it. The Tribunal is satisfied, however, that the aggressive nature of the attack going to issues of such gravity – the allegations of the fact of fraudulent accounting and the fact of insolvency – would have unnerved many general investors, causing them in all likelihood to sell Evergrande shares on the basis, if nothing else, that it was better to be safe than sorry.

275. In the judgment of the Tribunal, Mr Left, quite clearly, was intending just that effect. The whole tenor of the Citron Report supports that inference. More direct evidence, however, is to be found in the fact that, prior to the publication of the Citron Report, Mr Left set up a short selling mechanism. At all material times, therefore, he anticipated a drop in the share price, one from which he personally would be able to profit. This is not to condemn the profit motive. But it is a relevant factor in the present case. It is relevant because, as the Tribunal found in its Report, Mr Left was reckless as to whether the

allegations of fact made by him in the Citron Report were capable of being supported or not; put another way, he knew that there was a real risk that the central facts alleged by him – the facts of dishonest accounting and of insolvency – were false or misleading and yet he proceeded anyway, the evidence indicating that he took that action, in large part at least, because of the profit motive. That brings into the picture, when considering Mr Left's motives, an element of cynicism on his part, that the end justifies the means no matter what the collateral damage to general investors.

276. In coming to its determination, the Tribunal was at all times aware of the fact that the equity market is fluid, its dynamics changing from day to day. It was further at all times aware of the fact that the market is complex, multi-faceted and is therefore capable of being viewed in different lights. As such, opinions can differ widely and nevertheless all remain legitimate. S.277(1), however, does not seek to regulate opinions, not of themselves, not unless they are based on an assertion that is false or misleading as to a material fact. In the present case, the mischief perpetrated by Mr Left was not, therefore, related to his expressions of opinion, no matter the manner of their expression, the mischief was instead the assertions of fact made by him, assertions of fact drawn out from existing documents, that is, from historical data. These assertions of fact, however, could not – in all integrity – be made without an understanding of applicable accountancy standards and yet, on the evidence, it was apparent that Mr Left had taken no steps to ensure that his assertions of fact were made in the knowledge of those standards. For a professional in the field, bearing in mind the very serious nature of those assertions, this was recklessness of a gross nature. In the result, as the Tribunal

found, the allegations of fact displayed such an ignorance of the relevant accountancy regulations and standards that, in the opinion of one expert, a number of them constituted 'nonsense'.

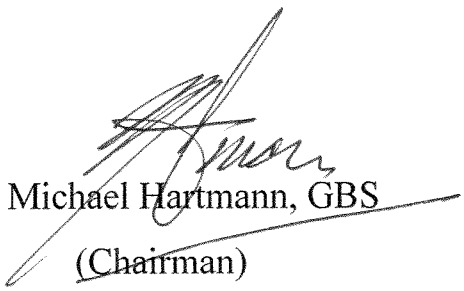
277. While the Tribunal may not have found that Mr Left *knew* that his factual allegations were false or misleading, nevertheless it was of the opinion that, in the circumstances of the present case, his recklessness was flagrant and gross. In this regard, it is to be remembered that the Citron Report was essentially based on an anonymous manuscript that Mr Left had received in the mail. As the Tribunal noted in its Report (paragraph 247):

> "… There was no indication therefore of the background of the author or his or her motives. Bearing in mind the sensationalist nature of the allegations made, it had to be as likely as not that the draft was penned by a person (or persons) bearing a grudge as it was penned by a person (or persons) seeking no more than an objective and fair exposition. Mr Left had many years of experience in publishing corporate commentaries, seemingly specializing in hunting down corporate fraud. He must therefore have appreciated that anonymous reports of this kind – making allegations of fraud, payment of bribes and other illegal dealings, required careful scrutiny. Indeed, it was Mr Left's case that he did go through a careful verification exercise …"

278. If that was the case, Mr Left would have appreciated that the allegations of fraudulent accounting and of insolvency, arising as they did, out of the audited accounts of Evergrande, were therefore rooted in an understanding of relevant accountancy standards and regulations. There was however, no

evidence whatsoever that Mr Left sought to publish The Citron Report in the knowledge of those standards and regulations. Was this naïveté on his part? Clearly not.

279. Mr Left, at the time he published the Citron Report, already had a reputation, one that he took pride it, for this type of attack. In paragraph 141 of the Report, the Tribunal has cited certain promotional material in which the Citron Research team said that, with over 150 reports, it had amassed a track record identifying fraud and terminal business models second to none. In paragraph 142, it has recorded the fact that Mr Left publicized the fact that he had successfully resisted a number of court actions arising out of his attack on companies. In considering whether the cold shoulder order should be imposed and, if so, for how long, the Tribunal took into account that the attack on Evergrande was not therefore a ‘one off’, it was part of a well-established procedure, one that in the circumstances was therefore more likely to be undertaken in the future if, in the view of Mr Left, a further opportunity presented itself.



Mr. Michael Hartmann, GBS
(Chairman)

Mr. Kwok Kam Hoi
(Member)

Dr. Wong Chak Sham, Michael
(Member)

Dated 10 November 2016