The report of the Market Misconduct Tribunal into dealings
in the shares of Yue Da Mining Holdings Limited
on and between 3 December 2007 to 12 September 2008

Part I : A report pursuant to section 252(3)(a) and (b) of the Securities and Futures Ordinance, Cap. 571

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CHAPTER 1

THE ISSUE OF THE FINANCIAL SECRETARY'S NOTICE AND ENSUING EVENTS

The Financial Secretary's Notice

1. The Tribunal was constituted in consequence of the Financial Secretary's Notice of 16 December 2011. The Notice was in the following terms.

"**IN THE MATTER OF THE**
SECURITIES AND FUTURES ORDINANCE (CAP 571)
AND
IN THE MATTER OF THE LISTED SECURITIES
OF YUE DA MINING HOLDINGS LIMITED
(STOCK CODE : 629)

NOTICE TO THE MARKET MISCONDUCT TRIBUNAL
PURSUANT TO SECTION 252(2) AND SCHEDULE 9 OF THE
SECURITIES AND FUTURES ORDINANCE, CAP 571
("THE ORDINANCE")

WHEREAS it appears to me that market misconduct within the meaning of Section 274 ("False Trading"), Section 275 ("Price Rigging") and/or Section 278 ("Stock Market Manipulation") of Part XIII of the Ordinance, has or may have taken place arising out of dealings in the securities of Yue Da Mining Holdings Limited (Stock Code 629) ("YDM"), the Market Misconduct Tribunal is hereby required to conduct proceedings and determine:-

(a) whether any market misconduct has taken place;

(b) the identity of every person who has engaged in market misconduct; and

(c) the amount of any profit gained or loss avoided, if any, as a result of the market misconduct.

Persons and/or Corporate Bodies Specified

Mr Li Libin ("Li"), Mr Qian Jinbiao ("Qian"), Yue Da Group (HK) Company Limited ("YDG (HK)"), Yue Da Mining Holdings Limited ("YDM"), and Mr Dong Liyong ("Dong").

Statement for institution of proceedings

1. At all material times, Li was a director and responsible officer of YDG (HK) which was the controlling shareholder of YDM holding more than 5% of YDM shares. YDG (HK) and YDM shared the same registered address in Hong Kong.

2. Dong was at all material times the Chief Executive Officer of YDM whereas Qian was the Company Secretary and Financial Controller of YDM.

3. At all material times, Li was an authorized signatory of the bank accounts of YDG (HK) and YDM.

4. At all material times, Qian was the authorized person to place orders for the securities trading account of YDG (HK) and YDM at the Bank of China International Holdings Limited ("BOCI").

5. In October and November 2007, YDM announced acquisitions of mining rights in the People's Republic of China ("PRC"). Between December 2007 and March 2008, YDM launched three placements of 20 million odd shares each (with top-up arrangement on two occasions) ("the Placements") to *inter alia* raise funds to finance the acquisitions. Dong and Li had prior knowledge of the Placements.

6. During the period on and between the 12th November 2007 and the 12th September 2008 ("relevant period"), YDG (HK), YDM, together with 4 accounts at the Hong Kong and Shanghai Banking Corporation

Limited ("HSBC") in the name of Zhang Hongyan ("ZH"), Su Linian ("Su"), Zhang Qing ("ZQ") and Cai Handong ("Cai") ("HSBC accounts") had aggressively traded in YDM shares.

Trades via the HSBC accounts

7. During the relevant period, Li operated and was the person responsible for making decisions of buying and selling YDM shares via the HSBC accounts of ZH, Su, and ZQ ("the Nominee Accounts").

8. Li operated and conducted trades of YDM shares during the relevant period via the Internet. The Internet Protocol ("IP") addresses showed that the YDM share orders during the relevant period via the Nominee Accounts were placed at different locations including the office of YDM/YDG (HK), Li's and Qian's residence.

9. The funding of the trades in YDM shares via the Nominee Accounts during the relevant period ultimately came from YDM.

10. The trading of YDM shares via the Nominee Accounts created a false appearance of strong market demand of YDM shares resulting in artificial support and/or increase in the price of YDM shares.

11. The trading of YDM shares via the Nominee Accounts did not involve any actual change in beneficial ownership.

12. Cai was the elder cousin of Dong. During the relevant period, Dong operated Cai's HSBC account.

13. The trading of YDM shares by Dong via Cai's HSBC account created a false appearance of strong market demand of YDM shares resulting in artificial support and/or increase in the price of YDM shares.

14. The trading of YDM shares by Dong via Cai's trading account did not involve any actual change in beneficial ownership.

Trades via YDG (HK)

15. During the relevant period, the decision to place orders of YDM shares via YDG (HK)'s BOCI account was made by Li.

16. Li would instruct Qian to place YDG (HK)'s orders for YDM shares during the relevant period.

17. The funding for the trading in YDM shares by YDG (HK) at the relevant period came from YDM's bank account.

18. The trading of YDM shares by YDG (HK) created a false appearance of strong market demand of YDM shares resulting in artificial support and/or increase in the price of YDM shares.

19. The trading of YDM shares by YDG (HK) did not involve any actual change in beneficial ownership.

Trades via YDM

20. During the relevant period, it was Dong's instructions and decision to repurchase YDM shares. Dong would instruct Qian to execute YDM's repurchase orders of YDM shares.

21. The trading of YDM shares by YDM created a false appearance of strong market demand of YDM shares resulting in artificial support and/or increase in the price of YDM shares.

22. Accordingly, Li, Qian, YDG (HK), YDM, and Dong engaged or may have engaged jointly or severally in market misconduct contrary to Sections 274, 275 and/or 278 of the Ordinance.

Dated this 16th day of December 2011

[Signed]
(John C Tsang)
Financial Secretary".

The amendment to the Notice

2. On 10 June 2013, at the beginning of the substantive hearing, Mr John Brewer, counsel representing two of the implicated parties (Yue Da Mining Holdings Limited and Mr Dong Liyong) objected to the inclusion in the Notice of paragraphs 13 and 14. He did so on the basis that these paragraphs were not supported by evidence, direct or indirect. The Presenting Officer, Mr Jonathan Kwan, conceded that there was insufficient evidence to support the assertions made in the two paragraphs and took no objection to their deletion from the Notice. In the result, having himself considered the issue of sufficiency of evidence, the Chairman, Mr Justice Hartmann, directed that the Notice be amended by the deletion of these two paragraphs together with certain incidental wording in paragraph 6 of the Notice. The amended Notice was signed on 2 July 2013 by the Chairman and members of the Tribunal.

The course of the proceedings

3. Before turning to the substance of this report, something must be said of the difficulties encountered in bringing the enquiry to a hearing and, on the evidence presented, to a determination by the Tribunal.

4. In January 2012, Mr Alan Wright, who had recently retired as a judge of the Court of First Instance, agreed to sit as Chairman of the enquiry.

5. As two of the specified persons, Mr Qian Jinbiao ("Mr Qian") and Mr Li Libin ("Mr Li") were resident in the Peoples' Republic of China (either the

"PRC" or the "Mainland"), the first directions hearing before the Chairman could only be held on 22 May 2012.

6. On that occasion, the Chairman was informed that the relevant documents together with the notice of the directions hearing which had been sent to the last known address of Mr Qian had been returned and endorsed to the effect that delivery had been refused. To avoid ambiguity, it should be said that it was later confirmed to the Tribunal that there had not been a failure to effect delivery because the address was unknown or was insufficiently detailed or because Mr Qian had moved addresses. The endorsement received from the PRC authorities was to the effect that delivery had been "refused".

7. The Chairman was further informed that Mr Li had only received the relevant documents together with the notice of the directions hearing the day before. Therefore, there had been no time to arrange for him to come to Hong Kong.

8. At this juncture it should be said that, while Mr Qian did not give a statement to the Securities and Futures Commission ("the SFC") and, so it would appear, refused to cooperate in any way whatsoever with the enquiry process, Mr Li, who at all times complained of serious ill-health, did give a statement to SFC officers and, although he said he was too ill to come to Hong Kong to appear before the Tribunal, agreed to give his evidence via video link from the Mainland. Arrangements were therefore put in hand to set up the necessary video link. As it was, however, after the commencement of the substantive hearing, by an email dated 2 July 2013, Mr Li informed the SFC that,

his health having deteriorated, he was to travel to Shanghai for further examination and treatment and would not be able to participate in the hearing by video link[1]. In the result, Mr Li did not give evidence either directly or by video link. He did, however, send a lengthy document under cover of an email dated 6 July 2013 in which he complained of the pressures put upon him by the enquiry and touched briefly upon the issues that fell for determination in this enquiry. This document ended with a request that he not be bothered any more in respect of the enquiry[2]. The contents of this document will be considered in greater detail in the body of this report.

9. At the first directions hearing held on 22 May 2012, the Chairman was informed that the SFC claimed privilege in respect of certain documents which counsel representing certain of the specified persons wished to examine. It was agreed that this preliminary issue would have to be dealt with before the commencement of the substantive enquiry which was set to commence on 5 November 2012 (with 25 days reserved). It was not possible to set an earlier date due to existing commitments of both the Chairman and counsel. As to the issue of privilege, this was settled at a further directions hearing held on 9 August 2012, it being agreed that a number (but not all) of the SFC documents would be made available for inspection.

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[1] The email (in translation) read as follows: "Sorry to inform you that the result of my examination at Yancheng Hospital a few days ago was not good. The doctor advised me to transfer to the hospital in Shanghai for further examination and treatment. So I cannot participate in the hearing as agreed."

[2] The document (in translation) ended with the following request: "Finally, once again I plead with you and hope that you can fully understand and respect my basic rights to health and not to disturb my treatment and living from now on. Besides, a long time has passed since the incident happened. Who can still remember those specific details? Even so, if I was to tell you about it again and again, only the same old story would be told. I beg the judge to consider my special situation and difficulties and those of my family and to exercise his discretion when deciding on my liabilities. Hence, please do not contact me any more by whatever means whether it is over the telephone, by email or through meetings etc."

10. At the hearing held on 9 August 2012, the Chairman directed that continued attempts be made to serve Mr Qian with relevant documents and notices. The Chairman accepted that it may be an exercise in futility but was of the view that, if an attempt was made to serve all relevant documentation upon him, Mr Qian could not be heard to complain at a later stage that he had been denied the opportunity to know of the progress of the enquiry and to be heard.

11. On 5 November 2012, this being the intended first day of the substantive hearing, the Chairman was informed of a number of difficulties that demanded that the hearing be adjourned. In this regard, the two principal difficulties were as follows.

12. First, it was said that an expert report prepared by Mr Eric Cheng, a former Senior Director of the Enforcement Division of the SFC, may contain fundamental miscalculations. The Presenting Officer, Mr Jonathan Kwan, informed the Chairman that he placed considerable weight on this report and said that he was not in a position to proceed until the issue of the miscalculations had been resolved.

13. Second, it was revealed that Mr Li, of whom earlier mention has been made, had been in email contact with the SFC explaining that he had undergone surgery for a form of cancer and had received treatment by way of chemotherapy. Despite these setbacks, however, Mr Li indicated that he wished to give evidence by way of video link.

14. It was agreed by counsel for the specified persons that the substantive hearing could not commence until the issue of Mr Cheng's report had been resolved. Counsel also agreed that, as Mr Li was potentially a very important witness – indeed in many respects perhaps the most crucial witness - attempts should be made to enable him to participate in the enquiry by way of video link.

15. The substantive hearing was adjourned for four days to enable the Chairman to receive an update on developments. At the adjourned hearing, it was apparent that amendments to Mr Cheng's report had resulted in the production of considerably more raw data which needed to be examined. In addition, the SFC needed more time to investigate the viability of setting up a video link to enable Mr Li to testify.

16. Accordingly, the matter of the enquiry was further adjourned to 23 November 2012 so that the Chairman could be appraised of developments. At that hearing, it was agreed that a substantive hearing would not be able to take place until well into the New Year. This meant that the Chairman would not be able to continue presiding as he had a number of prior commitments in the New Year.

17. The enquiry was therefore adjourned to 22 February 2013 to enable a new Chairman to be appointed. That Chairman was Mr Justice Hartmann who presided at the hearing on 22 February 2013. At that hearing it was agreed that the previous Chairman had not dealt with any matters concerning the merits of the enquiry and that accordingly there were no procedural barriers nor issues of

fairness that prevented Mr Justice Hartmann from assuming the role of Chairman.

18. At the directions hearing held on 22 February 2013 it was further agreed that the substantive enquiry should commence on 10 June 2013 (with 20 days reserved).

19. On 10 May 2013, one of the original members of the Tribunal, Mr Albert Wong Kwok Wai, submitted his resignation to the Financial Secretary. His resignation was brought about by the fact that, after the lengthy adjournments, he found himself in personal difficulties. In his place, Dr Norman Ngai Wai Yiu was appointed a member on 3 June 2013.

20. The substantive hearing commenced on 10 June 2013. There were limited interruptions to the sitting days due to the availability of witnesses and to certain prior travel arrangements on the part of the Tribunal members. However, the hearing was completed on 12 July 2013. The Tribunal had sat to receive evidence for a total of 16 days.

21. Having regard to the fact that almost all the counsel and the Tribunal members would be out of Hong Kong for the summer holiday period, it was agreed that the Presenting Officer would file his closing written submissions in early August 2013 while counsel representing the specified persons would file their submissions by the end of that month. As it was, all submissions were received by the Tribunal by mid-September 2013.

22. During the preparation of the report it became apparent that there were significant discrepancies between counsel as to the accuracy of the data related to the dealing in the shares of Yue Da Mining Holdings limited, more specifically the financial figures. Upon the completion of the first draft of the report it was apparent to the Chairman that the assistance of counsel was required in order to agree a set of accurate figures to be incorporated into the report. Accordingly, a letter dated 24 March 2014 was sent to counsel by the Secretary to the Tribunal. As to the fact that a first draft had been prepared, the Chairman made it plain that any determinations reached in that first draft were entirely provisional and that all aspects of the report would be considered afresh after accurate data had been settled by counsel.[3] The agreed figures are attached to this report as Annexure A (A1 – A15).

[3] The relevant portion of the letter reads: "… the Chairman has asked me to state again that a first draft of the report has been prepared. It was only in the preparation of the report that the true nature and extent of the discrepancies became apparent. Once an agreed table of figures is provided the final report can then be made available within a short period of time. The Chairman wishes it to be emphasised, however, that the Tribunal is not, and will not be, in a position to come to any final determinations until the agreed table has been submitted and has been considered by the Chairman and the members of the Tribunal in conjunction with all other relevant evidence. In this regard, the Chairman wishes it to be made clear that any determinations contained in the first draft are entirely provisional - indeed the draft determination still remain to be agreed by members of the tribunal - and will be considered afresh in each and every respect after the agreed table has been submitted."

CHAPTER 2

THE BACKGROUND

The Corporations and their inter-relationship

23. The focus of this enquiry has been on the dealings in the shares of Yue Da Mining Holdings Limited ("Yue Da Mining") which took place in the nine month period between 3 December 2007 and 12 September 2008, this period being called "the relevant period"[4]. In terms of the Financial Secretary's Notice, Yue Da Mining is a specified body.

24. Yue Da Mining was incorporated in the Cayman Islands in June 2001, its name at the date of incorporation being Yue Da Holdings Limited. It was only in late 2007, after the company began to acquire various mining rights in the PRC, that its name was changed to reflect its now dominant interest in mining.

25. Yue Da Mining was listed on the Hong Kong Stock Exchange under its original name in November 2001 (stock code 629). The company remains listed on the Stock Exchange, its principal areas of activity being the mining and processing of zinc, lead and iron and the management of toll highways and bridges in the PRC.

[4] There were initially differences as to the starting date of "the relevant period". However, it was agreed at the hearing that the correct starting date should be the one set out above, namely, 3 December 2007.

26. Yue Da Group (HK) Company Limited ("Yue Da Group (HK)") was incorporated in Hong Kong in September 1997. It was, and remains, the controlling shareholder of Yue Da Mining. At all material times the two companies had shared offices in Hong Kong. In terms of the Financial Secretary's Notice, Yue Da Group (HK) was a specified body.

27. Yue Da Group (HK) is itself wholly-owned by a PRC State Owned Enterprise comprising the Jiangsu Yueda Group of Company Limited ("the Jiangsu Group"). Founded in 1976, the Jiangsu Group is ultimately subject to the supervision of the Yancheng Municipal People's Government of Jiangsu Province. The evidence before us indicated that the Jiangsu Group employs over 30,000 people with business operations in Beijing and Shanghai and most of the Mainland's largest cities.

28. As the corporate architecture makes clear, Yue Da Mining is the Hong Kong listed arm of, and ultimately controlled by, the Jiangsu Group.

29. One further company should be mentioned at this stage, namely, the Yue Da Enterprise Group (HK) Company Limited ("Yue Da Enterprise"). As its name implies, it is a Hong Kong company. It is also wholly-owned by the Jiangsu Group. It would appear that all financial and/or accounting

transactions between Yue Da Mining and its controlling shareholder, Yue Da Group (HK), were accounted for in the current account of Yue Da Enterprise[5].

The key personalities

Hu You Lin ("Mr Hu")

30. At all material times, Mr Hu was the Chairman of the Board of Directors of the Jiangsu Group. He was the Chairman, Executive Director and founder of Yue Da Mining and a director of Yue Da Group (HK)[6]. Mr Hu was clearly, by reason of his office, responsible for making and/or approving major tactical decisions concerning all the corporations (in the Mainland and Hong Kong) falling under the umbrella of the Jiangsu Group. It appears that during the period of time which forms the central focus of this report Mr Hu was in poor health. He has since died.

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[5] Mr John Lees submitted an expert report dated 8 February 2013 in which he reviewed the accounting records of Yue Da Mining, its controlling shareholder, Yue Da Group (HK) and Yue Da Enterprise. In his review and analysis (at 2.2.2) he said: "The general ledgers of Yue Da Mining for the review period contain the current account of Yue Da Enterprise only. I have assumed that all transactions between Yue Da Mining and Yue Da Group (HK) were accounted for in the current account of Yue Da Enterprise. These assumptions were supported by the following observations.

3.1.4 I observed that Yue Da Mining made payments to Yue Da Enterprise and Yue Da Group (HK) either directly through its bank accounts (in the form of cheque or transfer) or through its subsidiary companies. These funds paid by Yue Da Mining and its subsidiary companies were then shown as a reduction in the current account payable to Yue Da Enterprise.

3.1.5 In addition, I noted that Yue Da Mining or its subsidiary companies made payments to individuals and third-party companies on behalf of the Jiangsu Group. These funds paid by Yue Da Mining and/or its subsidiaries were also shown as a reduction in the current account payable to Yue Da Enterprise.

3.1.6 Similarly, I observed funds received by the companies within the Yue Da Mining Group from Yue Da Group (HK), Yue Da Enterprise and its subsidiary companies (the Jiangsu Group). These funds received by Yue Da Mining were then charged to the inter-company account of Yue Da Enterprise.

3.1.7 I also noted there were transactions relating to payment of expenses (rental fees, staff salary, staff expenses etc) on behalf of Yue Da Mining which were then charged to the inter-company account of Yue Da Enterprise."

[6] The annual return dated 19 September 2007 reveals that there were two shareholders of Yue Da Group (HK), Mr Hu holding 1,485,000 ordinary shares with the balance of just 15,000 ordinary shares being held by a man who has played no role in this enquiry, Mr Gao Yishan.

Qian Jinbao ("Mr Qian")

31. We have earlier made reference to Mr Qian, he being the person who, on all appearances, declined to co-operate in any respect with this enquiry. At all material times, Mr Qian was the Company Secretary and Financial Controller of Yue Da Mining and, together with Mr Li Libin, was one of the authorised signatories of that company's bank accounts. He therefore held positions of authority with the publicly listed company, more especially in respect of its finances. Mr Qian was also an authorised signatory of the bank accounts of Yue Da Group (HK) and the person who actually operated the securities trading account of that company held with the Bank of China International Securities Ltd ("BOCI Securities") during the relevant period.

32. Mr Qian was from the Mainland, a veteran of the Jiangsu Group. The senior positions that were entrusted to him in respect of Yue Da Mining and Yue Da Group (HK) make it clear that he was trusted by the Jiangsu Group to execute financial strategies if not to originate them. On the evidence, the probabilities clearly indicate that he worked closely with Mr Li Libin, both being veterans of the Jiangsu Group transferred to Hong Kong. Whatever the true extent of Mr Qian's authority, whether he worked shoulder to shoulder with Mr Li Libin or perhaps as his subordinate, he was no mere cipher, blindly carrying out instructions. His positions of authority in *both* companies deny any such suggestion.

33. Mr Qian is a specified person.

Li Libin ("Mr Li")

34. We have also made reference earlier to Mr Li. He is the person who, because of ill-health, said that he could only give evidence by way of video link from the Mainland but who, shortly before he was scheduled to give his evidence, informed the Tribunal that he had to go to hospital in Shanghai and should not therefore be further disturbed.

35. Although Mr Li made a detailed statement to the SFC and spoke in some detail directly to the Tribunal by way of written communications, he remained an enigmatic character. As we have indicated, he too was a veteran of the Jiangsu Group and clearly trusted. Mr Dong Liyong (to whom we turn next) said that he was especially trusted by Mr Hu, the Chairman of the Board of Directors of the Jiangsu Group and "founder" of Yue Da Mining.

36. In his statements, Mr Li tended to play down the degree of his involvement in the strategic operation of Yue Da Mining and Yue Da Group (HK) but, in our opinion, having viewed the evidence as a whole, it is apparent that he was very much "the power behind the throne".

37. Mr Li was a director of Yue Da Group (HK), the controlling shareholder of Yue Da Mining and, on the evidence, the responsible officer of that company. He was an authorized signatory of the bank accounts of that company. That position alone put him in a position of considerable influence as to the affairs of Yue Da Mining. More than that, he was also an authorized signatory of the Yue Da Mining bank accounts together with Mr Qian, a fellow veteran of the Jiangsu Group. By contrast, Mr Dong Liyong, the CEO of Yue

Da Mining was not an authorized signatory of his own company's bank accounts. Admittedly, Mr Li was not a director of Yue Da Mining but he still fulfilled certain public relations functions on behalf of the company. On any objective view, therefore, Mr Li was strategically positioned not to partake in the day-to-day management of Yue Da Mining, that being the responsibility of Mr Dong Liyong, but to devise and execute financial plans that may affect Yue Da Mining and/or other companies in the Jiangsu Group.

38. One such strategic plan might have been the maintenance of the share price of Yue Da Mining at a critical time in its corporate history as it was transforming itself into a major player in the Mainland mining sector and required to raise very large sums to pay for its acquisitions. In this regard, it is notable that Mr Li knew of and/or authorized the purchase of Yue Da Mining shares by Yue Da Group (HK) at or about the same time as he was, on his own admission, using certain "nominee" accounts to actively deal in the same shares. More than that, on the face of it at least, it defies common sense to think that he knew nothing of the share buy-back exercise executed by Yue Da Mining in January 2008. He shared offices with Yue Da Mining; he worked with Mr Qian who was the Financial Controller of Yue Da Mining, and he was a bank signatory - to the exclusion of the CEO himself. In addition, if the evidence of Mr Dong Liyong is accepted, he was much trusted by Mr Hu, the head of the Jiangsu Group, who authorized the share repurchase scheme. We shall of course look more closely to the evidence related to Mr Li but, at this early juncture, on the face of it at least, he appears to have been well positioned to execute a scheme to maintain Yue Da Mining's share price.

39. Mr Li is a specified person.

Dong Liyong ("Mr Dong")

40. At all material times, Mr Dong was an executive director, vice-chairman and chief executive officer ("CEO") of Yue Da Mining, having taken up the post of vice-chairman and CEO in January 2007. Mr Dong took up residence in Hong Kong in 1996. He is a graduate of Renmin University, Beijing, and holds an MBA from the University of California at Berkeley.

41. A matter emphasised on behalf of Mr Dong was that, unlike other directors and senior officers of Yue Da Mining and its associated companies, he was not appointed by way of secondment from the Jiangsu Group but was engaged directly on the invitation of Mr Hu because of his knowledge of good corporate governance and the relevant laws and regulations of Hong Kong. As such, his appointment was not subject to Jiangsu Group approval.

42. A matter further emphasised on behalf of Mr Dong was that, as he was not seconded from the Jiangsu Group, despite holding the most senior executive office with Yue Da Mining, he was not entrusted with cheque signing authority until after September 2008.[7] As Mr Dong explained it in paragraph 9 of his statement dated 7 June 2013: "… such signatory power had been restricted to expatriate colleagues such as Li Libin [Mr Li] and Qian Jinbiao [Mr Qian] holding office with the Jiangsu Group specifically so that the Jiangsu Group

[7] He was however given authority to sign vouchers supporting financial transactions.

could be sure of monitoring and exercising control over the Company's cash balances."

43. Mr Dong is a specified person.

A short history of Yue Da Mining: from road tolls to mining exploitation

44. On 8 October 2007, Yue Da Mining announced that it was in negotiations concerning the acquisition of mining rights (of zinc and lead ores) in the Shaanxi Province.

45. This was the first public indication that the company was moving from its then principal business, namely, the management of road and bridge tolls, into the mining sector.

46. In the 21 months prior to that announcement, the Hang Seng Index had risen by about 83%. In that same period, shares of Yue Da Mining had traded between HK$0.58, this being the closing price on 4 January 2006, and HK$5.70, this being the intra-day high on 29 May 2007. On the day before the announcement of 8 October 2007, the share had closed at HK$4.78. During this 21-month period the average daily turnover had been in the region of 758,000 shares.

47. Initially at least, the announcement that the company was moving into the mining sector was well received by the market. Shares of the company reached a high of HK$6.30 before falling back to HK$5.90 immediately before it was announced that the acquisition agreement had been concluded.

48. On 18 October 2007 it was confirmed that an agreement had been entered into to purchase the Shaanxi Province mining rights for a sum of HK$120 million, the purchase price to be funded by internal resources and debt financing.

49. A month later, on 19 November 2007, a suspension of trading was announced pending the publication of details concerning the acquisition of further, more extensive mining rights.

50. On 30 November 2007 it was announced that these more extensive mining rights had been secured ("the Inner Mongolia mining rights") for a consideration of HK$299 million and RMB830 million[8]. As to the funding of these two amounts, it was announced that it would be raised by internal resources and equity and/or debt financing. In particular, it was said that Yue Da Mining was considering different financial proposals but had not yet made its final decision. Further announcements would be made when a decision as to the nature of such financing had been decided upon in accordance with the requirements of the Listing Rules[9].

51. On 3 December 2007 - after the announcement of 30 November that heralded the transformation of the company into a major player in the

[8] In a letter to the SFC dated 29 February 2008, Yue Da Mining said that in aggregate the purchase price amounted to over RMB1,105 million.

[9] In its letter to the SFC dated 29 February 2008, Yue Da Mining said in respect of the consideration of over RMB1,105 million for the Inner Mongolia mining rights: "As shown in the Company's interim report published in late September 2007, the Group's total current assets as at 30 June 2007 amounted to some RMB52 million. It was clear that the group would need external financing to pay the said considerations."

Mainland's mining sector - shares of Yue Da Mining peaked at an all-time high of HK$9.00[10] before slipping back to close the day at HK$8.02.

52. A week later, however, by 10 December 2007, Yue Da Mining shares had slipped below HK$7.00[11], closing that day at HK$6.90, and thereafter were to remain below the HK$7.00 level.

53. Having shifted the emphasis of its business activities to mining, the company resolved to change its name to reflect the shift, the formal announcement of the change being made in January 2008.

The first share placement

54. In making its transformation from a company involved in the operation of toll roads and bridges to a major player in the Mainland's mining sector, Yue Da Mining had acquired very considerable debt, debt that it was not able to pay from its own resources. As the announcement of 30 November 2007 had made clear, in order to meet the costs of the mining acquisitions and to provide for working capital, "equity and/or debt financing" was needed.

55. On 7 December 2007, share trading having been suspended on the day before, Yue Da Mining announced that it had entered into what is commonly called a top-up placing agreement. The agreement was with its major

[10] On a trading volume of 1,071,000 shares and a turnover of HK$8,368,310.00.

[11] On a very high volume that day of 30,292,000 and a turnover of HK$201,040,990.00.

shareholder, Yue Da Group (HK) and a placing agent[12]. The agreement was for the placing of 20 million existing Yue Da Mining shares at a discounted price of HK$6.63 per share to independent investors. Yue Da Group (HK) advanced those 20 million shares. The top-up element of the agreement was the provision that Yue Da Group (HK) would subscribe for an equal number of new shares at the same price to be issued by Yue Da Mining. The published purpose of this top-up placing exercise was to finance the mining acquisitions and also to meet the requirements of general working capital.

56. Even though, in terms of the top-up placing exercise, Yue Da Group (HK) was able to reclaim the same number of shares that it had advanced and at the same price, with more issued shares now in existence its percentage shareholding of all issued shares had been diluted, dropping from 47.93% to 44.78%. This represented a drop of 3.15%.

Yue Da Group (HK) purchase of Yue Da Mining shares

57. In December 2007, 451,000 shares were purchased by Yue Da Group (HK) at a cost of HK$3,046,099.17. In January 2008, 284,000 shares were purchased at a cost of HK$1,799,555.53. In February 2008, a further 2,590,000 shares were purchased at a cost of HK$13,533,867.56[13].

58. The purchases were managed by Mr Qian using the trading account held with BOCI Securities. Whatever general instructions he may have

[12] The placing agent was Piper Jaffray Asia Securities Limited.

[13] Yue Da Group (HK) engaged in a further exercise of purchasing Yue Da Mining shares between 15 April and 24 June 2008.

received, it was Mr Qian therefore who determined on a day by day basis when to buy, at what price and in what quantities.

59. During the course of the hearing, the Tribunal was asked to consider whether, in the context of the broader picture of all the share trading identified in the Financial Secretary's Notice, funds had been purposefully channelled from Yue Da Mining directly or indirectly to Yue Da Group (HK) to enable it to make the purchases for the specific purpose of increasing and/or stabilising the price of Yue Da Mining shares at an uncertain time of transition in the company's history. On behalf of Yue Da Group (HK) this was denied. These purchases, it was submitted, represented genuine efforts on the part of Yue Da Group (HK) to increase its shareholding after it had been diluted in the top-up placement exercise. It was submitted that the decision was made by Mr Hu, Chairman of both the Jiangsu Group and Yue Da Mining, and was executed by Mr Li with the assistance of Mr Qian.

60. It was submitted that the money used to purchase the shares, that money being paid to BOCI, was represented by six deposits made between 27 December 2007 and 25 April 2008[14]. One of the deposits, it was said, came from Yue Da Mining's own funds, the other five were all repayments of debts due by Yue Da Mining to Yue Da Group (HK). In short, there was nothing about the fund flow capable of raising concerns. As between associated companies, it was part of the normal ebb and flow of finances.

[14] The six deposits were as follows. First, HK$5 million paid on 27 December 2007; second, HK$4,999,990.00 paid on 31 January 2008; third HK$4,999,990.00 paid on 14 February 2008; fourth HK$3,999,990.00 paid on 18 February 2008; fifth HK$999,900.00 paid on 24 April 2008 and, sixth, HK$1,999,990.00 paid on 25 April 2008 stop.

61. It was submitted by Mr Keith Yeung SC, leading counsel for Yue Da Group (HK) that we should at all times be aware of the fundamental fact that Yue Da Group (HK) was at full liberty to deal with and in the shares of Yue Da Mining. In that regard, its position was no different from that of any third-party investor. It was not constrained by a prescriptive regulatory regime as Yue Da Mining was when purchasing its own shares.

62. We pause at this juncture to say that, in our view, while obviously the source of funding and the context in which it is made available is an important factor, and may indeed be decisive, the true issue is not the "legitimacy" of funds used but the intention with which they are deployed.

63. Accordingly, if for the sole or primary purpose of supporting a share price (thereby undermining the interplay of genuine market forces), a company builds a war chest by calling in loans that are properly due and/or raises funds by way of loans from associated companies, and then employs those funds for the intended purpose, it seems to us that the company may nevertheless be culpable of a manipulation of the market.

<u>The buy-back by Yue Da Mining</u>

64. Some 10 days before Yue Da Group (HK) ceased its exercise of purchasing Yue Da Mining shares, Yue Da Mining itself began to repurchase its own shares. This exercise ran for a period of five trading days from 16 January

to 23 January 2008. In this period, a total of 862,000 shares were purchased at a cost of HK$4,912,042.68.[15]

65. On 16 January 2008, Yue Da Mining shares closed the day at HK$6.00[16]. On 23 January 2008, they closed the day at HK$5.40, a drop in the price in the repurchasing period of 60 cents.

66. In the same period, the Hang Seng Index had declined from 24,450.85 to 24,090.17.

67. As to why the repurchase took place, Mr Dong, the CEO of Yue Da Mining, testified that on Saturday, 12 January 2008 he communicated with Mr Hu, Chairman of the Jiangsu Group and of Yue Da Mining itself, to express concerns that, despite the transformation of Yue Da Mining, the share price remained undervalued. He recommended that a sum of up to HK$10 million be employed to repurchase Yue Da Mining shares. It was the essential thrust of Mr Dong's evidence that he wished to signal to the market that the senior management of Yue Da Mining was optimistic as to the company's prospects. Mr Hu gave permission. Mr Dong said that he instructed Mr Qian to proceed

[15] These figures are obtained from the five Form Gs submitted to the Stock Exchange by Yue Da Mining. The forms declare the following. First, on 16 January 2008, 249,000 shares were purchased for HK$1,473,820.00; second, on 17 January 2008, 162,000 shares were purchased for HK$972,000.00; third, on 21 January 2008, 117,000 shares were purchased for HK$700,800.00; fourth, on 22 January 2008, 220,000 shares were purchased for HK$1,141,450.00, and, fifth, on 23 January 2008, 114,000 shares were purchased for HK$606,400.00.

[16] On a volume of 8,536,000 shares and a turnover of HK$54,848,795.00 to be contrasted with a volume of just 81,000 the day before and a turnover of HK$524,250.00.

with the repurchase exercise.[17] Again, therefore, Mr Qian was charged with the detailed discretion of when to buy, at what price and in what quantities.

68. Concerning the purpose of the repurchase exercise, in a letter dated 29 February 2008 to the SFC, it was said that on 14 January 2008 Yue Da Mining shares had fallen to HK$5.00 per share, this price to be compared with the closing price of the shares in December 2007 when they were generally over HK$6.00 per share. It was the view of senior management that the repurchase exercise would enhance the net asset value per share, restoring the confidence of shareholders and would thereby be of benefit generally to the company and to its shareholders.

69. A listed company is permitted to purchase its own shares but only in strict accordance with a prescriptive regulatory regime. During the course of the hearing, it was accepted that the repurchase exercise had been in compliance with the terms of that prescriptive regime. The share repurchases were fully disclosed to the Stock Exchange and to the market.

70. Mr Ermanno Pascutto, an expert on the matter of listed companies repurchasing their shares, submitted a detailed report and gave evidence by way of video link from Canada. His evidence was restricted to the repurchase exercise itself. He did not seek to place that exercise in any broader context.

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[17] As to the repurchase exercise, Yue Da Mining advised the SFC (in its letter of 29 February 2008) that: "… the decision was generally made by Mr Dong, an executive director. With the instruction from Mr Dong, Mr Qian, the company secretary and qualified accountant of the company, called up Ms Joyce Wong and other officers assisting her of BOCI to effect the repurchase transactions. The repurchase prices for the repurchase transactions were determined by reference to the then prevailing market prices of the shares."

On this limited basis, it was his evidence that the share repurchasing exercise, because it was in accordance with the prescriptive regime, did not constitute any form of market manipulation. It was his evidence that, even if the share repurchase exercise was intended to support the share price, in terms of the prescriptive regime that was a proper motive and was permitted.

71. We shall look in greater detail to Mr Pascutto's evidence later in this report. At this stage, however, we can say that we found it to be convincing.

72. That, however, has not disposed of the issue of whether the share repurchase exercise, even if in itself it was legitimate, when considered in the broader context, constituted a device or ploy intended to manipulate the market.

73. In this regard, we were asked to consider the fact that a second share placement took place literally within hours of the share repurchase exercise being abruptly concluded. Was the share repurchase exercise undertaken in the knowledge of that second placement exercise, an exercise that was not made known to the market? If so, the company was repurchasing its shares at a time when it was in possession of price sensitive information[18] and that must constitute market misconduct.

74. On a broader basis, even if it was found that the share repurchase exercise in itself was legitimate, as part of a far broader strategy, did it constitute market manipulation? In determining this issue, we were asked to take into

[18] On 24 January 2008, Yue Da Mining announced that trading in its shares was suspended pending the release of an announcement considered to be price sensitive. The announcement gave details of the second share placement.

account that Yue Da Group (HK), Yue Da Mining's controlling shareholder, had just concluded a share purchasing exercise and that, at about the same time, Mr Li began to deal actively in the shares of Yue Da Mining in a disguised manner by using several "nominee" accounts. Taken together, it was suggested that what was revealed was a strategy to hold up the share price at a time when the company was actively seeking to raise equity capital.

The second share placement

75. Considered in the light of the issues to which we have just referred, evidence relevant to the second share placement takes on importance. Of particular importance, in our view, is the issue of whether, in regard to the share repurchase exercise, it was undertaken when senior management knew that a second placement exercise was imminent or that such an exercise (or one of a similar nature) would have to be conducted in the immediate future.

76. As to the second share placement, the most detailed history of relevant events was put before us by Mr Dong. It speaks for itself, of course, that in considering what weight, if any, we could give to that history we looked to evidence that supported it and evidence that tended to undermine its truthfulness and/or accuracy.

77. On its face, it is puzzling that, although it was intended to spend up to $10 million on the repurchase exercise, instructions were given to cease the exercise within a matter of days and at a time when less than half of the HK$10 million had been expended.

78. Mr Dong gave evidence that the share repurchase exercise ended abruptly because unexpected events intervened.

79. The first unexpected event was the news that certain legal formalities in respect of the Inner Mongolia mining rights had been concluded earlier than expected and that a payment of HK$100 million had to be made within a matter of days, that is, before the end of January 2008.

80. The second unexpected event was the fortuitous approach by a finance company, SBI-E2 Capital. In this regard, it was the evidence of Mr Dong that on the evening of 23 January 2008, when he was still digesting the news that a sum of HK$100 million had to be raised without delay, he was contacted by a Ms Vivian Ip Hung of SBI-E2 Capital, a woman with whom he had earlier had discussions of a general nature only about the possibility - and no more - of raising capital by way of a further placement exercise. On the earlier occasions, said Mr Dong, he deflected the approach, saying that a further placement exercise was unlikely, especially having regard to the sluggish condition of the market. On the evening of 23 January 2008, however, Ms Ip informed him that, as the market appeared to be stabilising, she believed it would be possible to conduct a further placement exercise with the shares priced at between HK$5.20 and HK$5.40.

81. Mr Dong said that he reported the approach that same evening to Mr Hu, obtaining his approval to raise HK$100 million by way of a further placement of 20 million shares but on this occasion with no discount. The price was to be HK$5.40 per share or better. It was Mr Dong's evidence that

he relayed the matter to Ms Ip who - that same evening - was able to confirm that there was sufficient interest to enable the placing exercise to go ahead.

82. For that reason, said Mr Dong, he gave instructions to Mr Qian to immediately cease the repurchase exercise and the following morning he instructed the company's solicitors to make submissions to the Stock Exchange in respect of the intended second placement exercise.

83. As to this history, we have earlier said that we looked for other evidence to support it or to undermine it. Supporting evidence was found in the form of Ms Ip's evidence. It was also found in the form of effectively contemporaneous communications between Yue Da Mining's solicitors and the Stock Exchange. This is because within about 48 hours of the events which Mr Dong described as taking place on 23 January 2008 those same events were being referred to in the communications.

84. The reason for the communications with the Stock Exchange arose out of the fact that Yue Da Mining was seeking, within a period of 30 days after repurchasing its own shares, to issue new shares. That was permissible but only if the Stock Exchange agreed. The Stock Exchange was informed that Yue Da Mining, its controlling shareholder, Yue Da Group (HK) and a placing agent, SBI-E2 Capital, had entered into an agreement for the placing of 20 million existing shares at a price of HK$5.40 per share to independent investors. The agreement included a conditional provision that Yue Da Group (HK) had agreed to subscribe for an equal number of new shares to be issued by Yue Da Mining at the same price, this being the top-up element of the agreement.

85. As it was, the Stock Exchange refused to give consent. In light of this decision, the top-up element of the second placement exercise had to be cancelled.

86. On 29 January 2008, share trading having been suspended from 24 January 2008 (during which time the solicitors for Yue Da Mining had attempted to persuade the Stock Exchange to permit the top-up element of the new placement of shares), Yue Da Mining announced the second placement exercise in respect of 20 million shares at a price of HK$5.40 per share. The announcement stated that the original intention had been for a second top-up placement but that the Stock Exchange had not consented to this.[19]

87. Between the first and second share placements, Yue Da Group (HK) had increased its percentage shareholding in Yue Da Mining by the relatively insignificant percentage of 0.14%. However, after the second placement, with there being no top-up element, the percentage shareholding fell by over 6% to 38.35%.

The third share placement

88. A final, third share placement took place on 19 March 2008, some six weeks after the second placement. On this occasion, Yue Da Mining announced a third placing agreement in respect of a further 20 million shares,

[19] In this regard, the announcement said: "… as the Company has recently carried out the repurchase transactions and the Stock Exchange has not granted approval under Rule 10.06 (3) of the Listing Rules, the Company cannot proceed with the proposed issue of new shares under the subscription agreement and accordingly the subscription agreement was cancelled on 29 January 2008."

this time at a price of only HK$5.00 per share. On this occasion there does not appear to have been any named placing agent. Yue Da Group (HK) was the vendor but there does not appear to have been any top up. The 20 million shares were taken up by Value Added Partners Limited, a company involved in investment management.

89. Following this third placement, it was anticipated that the percentage shareholding of Yue Da Group (HK) would be further reduced to 36.89%.

90. As Mr Yeung, counsel for Yue Da Group (HK) pointed out, the three placement exercises had resulted in a dilution of the company's overall percentage shareholding of over 10%. In this regard, he commented that it would make good commercial sense for a major shareholder, particularly in respect of a state-owned enterprise, to increase its shareholding in order to better secure its position as controlling shareholder.

91. As it was, between 24 April and 24 June 2008, Yue Da Group (HK) purchased 740,000 shares in Yue Da Mining for a sum of HK$3,606,570.12. On the evidence, it appears that these purchases were (in the main) settled by two payments: one made on 24 April 2008 in the sum of HK$999,900.00 and one the following day in the sum of HK$1,999,990.00. The accounting voucher of Yue Da Mining of 24 April 2008 records the payment as coming via Yue Da Enterprise, the second payment appears to have been withdrawn from one of Yue Da Mining's bank accounts, the voucher recording: "other payables/Yue Da Enterprise…".

92. The evidence put before us was to the effect that it was the invariable practice that such entries were made through Yue Da Enterprise.[20] In this regard, Mr Yeung summarised the evidence of Mr John Lees (given as an accounting expert) in the following terms:

> "He confirmed that from the Group's current accounts, there were flows of money from one company to the other which, in effect, were repayments of debts owed and advancements of working capital. It was common that the purposes were not stated on accompanying vouchers, but the overall view would reflect the credit and debit for each company. Mr Lees also testified that he did not find it strange to have the accounts arranged in such a manner. Any credit entries made to the current account of Yue Da Mining in the books of Yue Da Enterprise would represent a repayment of loan."

Dealing in Yue Da Mining shares through the "nominee" accounts

93. In a statement given to the SFC in the Mainland on 13 March 2009, Mr Li admitted that he had used three so-called "nominee accounts", each held with HSBC in Hong Kong, to deal in Yue Da Mining shares. The dealing took place between 3 December 2007 and 12 September 2008. To employ his expression, Mr Li said that he had "borrowed" the accounts in order to "purchase shares for my friends". The accounts were in the name of three women. There was no evidence that any of them used the accounts for their own trading. How the accounts came to be created may be summarised as follows:

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[20] Mr Bai Zhaoxiang, who joined Yue Da Mining in November 2007, being stationed in Kunming, and who at the time that he gave evidence was the Financial Controller of Yue Da Mining and an Executive Assistant Director, said the following in a statement made to the SFC in January 2009 : "I want to tell you that, actually, the fund transfers between Yue Da Mining and Yue Da Group (HK) were sometimes for the lending of money by Yue Da Group (HK) to Yue Da Mining and sometimes for the repayment of money by Yue Da Mining to Yue Da Group (HK). But, in most cases, when funds were transferred by Yue Da Mining to Yue Da Group (HK)'s bank accounts, accounting entries were actually made through Yue Da Enterprise for financial treatment purposes. In the case of loans from Yue Da Group (HK) to Yue Da Mining, accounting entries were also made through Yue Da Enterprise for financial treatment purposes."

i. Zhang Hongyan was an employee of the Jiangsu Group working in human resources. She got to know Mr Li and came with him to Hong Kong on a business trip. While here she was asked by Mr Li to open her HSBC trading account. The account was opened on 3 February 2006.

ii. Su Linian used to work as a service attendant on trains. She came to know a man by the name of Wu Guoyi ("Mr Wu") who she understood had diverse business interests in the Mainland. Mr Wu and Mr Li arranged to bring her to Hong Kong and during her time here she was asked by Mr Li to open her HSBC trading account. The account was opened on 22 February 2006.

iii. Zhang Qing was variously described as a babysitter or governess. Mr Li assisted her to come to Hong Kong and persuaded her to open an HSBC trading account. He apparently said to her that the account was being opened to assist a friend, Mr Jiang Chun, the Deputy General Manager of a Mainland corporation called Nanjing Zhongxinyue. The account was opened on 16 March 2007.

94. During the course of the enquiry, the accounts opened by the three women with HSBC were described as "nominee" accounts. This was little more than a convenient shorthand expression. A nominee is a person appointed by another to act on his or her behalf. Mr Li was never appointed by any of the three women to act on their behalf. He used the three women to set up trading accounts which he was then able to operate for his own benefit and/or the benefit of his associates without any reference back to them. It was a convenient form of disguised trading.

95. Trading in Zhang Hongyan's account took place between 3 December 2007 and 13 February 2008. All the trading was in Yue Da Mining shares. Between those dates a total of 1,388,000 shares were purchased at an average purchasing price of some HK$7.79 per share and 680,000 shares were sold, leaving a credit of 708,000 shares. Those 708,000 shares cost Mr Li a sum of HK$5,576,976.00. During the trading period the account was used to trade not just on one or two days but on 36 out of 42 trading days: there was therefore a regular pattern of dealing.

96. Trading in Su Linian's account took place between 2 January and 22 April 2008. All the trading was in Yue Da Mining shares. In that period, a total of 994,000 shares were purchased. No sell orders were placed. These 994,000 shares cost Mr Li a sum of HK$4,992,631.06. Between 26 February and 22 April 2008, when the great bulk of the trading took place, Mr Li traded on 27 out of 37 trading days. Again, there was a regular pattern of trading.

97. Trading in Zhang Qing's account took place between 15 April and 12 September 2008. All the trading was in Yue Da Mining shares. Between these dates a total of 1,662,000 shares were purchased at an average purchasing price of some HK$3.18 per share and 56,000 shares were sold, leaving a credit of 1,606,000 shares. These 1,606,000 shares cost Mr Li a sum of HK$5,143,277.11. During the trading period, Mr Li traded on 66 out of the 103 trading days. Trading in this account was over a longer span of time than in the other two "nominee" accounts but it was still fairly regular: dealing took place on well over half the trading days.

98. It can be seen that trading in the three accounts overlapped. Trading in Zhang Hongyan's account took place between 3 December 2007 and 13 February 2008. Trading in Su Linian's account took place between 2 January and 22 April 2008. Trading in Zhang Qing's account took place between 15 April and 12 September 2008.

99. During the course of the enquiry nothing was put before us to suggest that there was any particular reason for trading in one particular account at one particular time. It was not suggested, for example, that Zhang Hongyan's account was reserved for one particular "friend" while Su Linian's account was reserved for another.

100. Clearly, the dominant purpose of trading in all three accounts was to acquire Yue Da Mining shares not directly to trade (i.e. to buy and sell) for purposes of profit. Between 3 December 2007 and 12 September 2008, this being the total trading period in respect of all three accounts, Mr Li purchased through the "nominee" accounts 4,044,000 shares, selling 736,000. This left a purchase "credit" of 3,308,000 shares.

101. The regular occurrence of dealing in all three accounts is also indicative, more especially as the dominant purpose of the dealing was to acquire Yue Da Mining shares despite the fact that on a month by month basis, although the share price stabilised for limited periods, the overall pattern was one of weakening.[21]

[21] By way of example, in December 2007, the share price fell from HK$8.020 to HK$6.770; in January 2008 it fell to HK$5.34; in February 2008 it remained stable, closing at $5.34; in March 2008 it fell to HK$4.89.

102. We will come shortly to Mr Li's explanation for his dealing. Essentially, however, he was dealing on behalf of others, he said, for investment purposes. Put simply, he was not dealing with his own money; the funds he used to deal belonged to others: one company in particular, supposedly an entity independent of the Jiangsu Group. There is no suggestion on the evidence put before us that he was under strict instructions to deal only in Yue Da Mining shares. Yet there is no evidence that at any time he suggested to those who had entrusted him to invest on their behalf that perhaps the portfolio should be broadened or that they had suggested the same to him. Instead, persistently and by way of a regular pattern of dealing, Mr Li purchased Yue Da Mining shares and only Yue Da Mining shares. To the cynic, it suggests either a wilfully blinkered approach or an intent to deal with some ulterior motive.

103. As to the patterns of dealing, by way of an overview, the following can be said.

i. On 3 December 2007, the end of the first day of trading in Zhang Hongyan's account, Yue Da Mining shares closed at HK$8.02 on a turnover of HK$8,369,310.00. On 13 February 2008, the last day of trading in that account, the shares closed at HK$5.85 on a turnover of HK$176,500.00. In the time it took Mr Li to acquire his 708,000 shares (the net share credit at the end of 13 February 2008) in this account, their price had fallen by HK$2.17.

ii. On 2 January 2008, the end of the first day of trading in Su Linian's account, Yue Da Mining shares closed at HK$6.63 on a turnover of HK$1,278,800.00. On 22 April 2008, the last day of trading in that

account, the shares closed at HK$4.90 on a turnover of HK$855,900.00. In the time it took Mr Li to acquire his 994,000 shares in this account, their price had fallen by HK$1.73.

iii. On 15 April 2008, the end of the first day of trading in Zhang Qing's account, Yue Da Mining shares closed at HK$4.95 on a turnover of HK$604,910.00. On 12 September 2008, the end of the last day of trading in the account, the shares closed at just HK$1.80 on a turnover of HK$828,520.00. In the time it took Mr Li to acquire his 1,606,000 shares (the net share credit at the end of 12 September 2008), their price had fallen by HK$3.15.

104. To give some perspective to these figures, between 3 December 2007 and 12 September 2008 (inclusive) the value of Yue Da Mining shares slumped from HK$8.02 to HK$1.80, a drop of some 77%. Seen over that same period, the Hong Kong market also suffered a marked decline, the Hang Seng Index moving from 28,658.42 to 19,352.90, a drop of just under 33%. Even accepting that Yue Da Mining shares were not blue chip and therefore subject to more extreme degrees of volatility, a comparison with the decline in the Hang Seng Index nevertheless serves to indicate just how precipitous was the decline in the value of Yue Da Mining shares.

<u>What then was the explanation for the trading in these accounts by Mr Li?</u>

105. In his interview with the SFC given on 13 March 2009, Mr Li said the following:

> "I was entrusted by Mr Jiang of Nanjing Zhongxinyue Company to operate the accounts. As he was not familiar with the operation of the Hong Kong

> stock market and it was not easy for him to access the Internet when he ran around outside doing business the whole day, I was entrusted to operate the accounts via the Internet for him."

106. As to the source of the funding, Mr Li said the following:

> "It was me who withdrew money from the accounts of Yue Da Enterprises (or Yue Da Mining) and then transferred it to them. The ultimate source of the funds came from the repayment of the amount due to Nanjing Zhongxinyue Company by Yue Da Enterprises on behalf of the Jiangsu Group. In other words, it is Nanjing Zhongxinyue's Company's money. Such a funding arrangement was approved by Liu Yadong, head of the finance department of the Jiangsu Group after mutual negotiations. Otherwise I would definitely not dare to withdraw such a large amount of money privately and bear the responsibility. I can assure you that I have never gained a cent from it."

107. As to the exact source of the funds, Mr Li said that it was agreed that repayment would be made by Yue Da Enterprises. The exact details of the source of the funds and their movements, he said, were to be found in the relevant corporate accounts.

108. Mr Li said that it was Mr Jiang who took delivery of the 768,000 and 1,768,000 Yue Da Mining shares withdrawn respectively from the Zhang Hongyan and Su Linian HSBC accounts in June 2008.

109. On 11 March 2009, the SFC interviewed Mr Jiang Chun himself, doing so in Nanjing. At the time of the interview, he said that he held the post of Deputy General Manager of Nanjing Zhongxinyue Trade and Industry Development Company ("Nanjing Zhongxinyue") and had been with the company since 2006.

110. Mr Jiang said Nanjing Zhongxinyue was at one time a subsidiary of the Jiangsu Group but had been the subject of a restructure so that at the material time it was owned and controlled by four shareholders, three individuals and a company which appears to have been part of the Jiangsu Group; namely, Jiangsu Yue Da South Holding Company Limited (which had a 4% holding).

111. Mr Jiang said that in 2007 Mr Wu Guoyi[22] (who appears to have had business interests in Sichuan but whose company name Mr Jiang could not remember) was indebted to Nanjing Zhongxinyue and suggested that he repay the debt by transferring Yue Da Mining shares. In October 2007, after discussions, it was agreed that something like 800,000 shares would be transferred at a value of approximately RMB 3 million.

112. In respect of the transfer of shares, Mr Jiang said that he was informed by Mr Wu that his shares were held in the name of two "nominees", namely, Zhang Hongyan and Su Linian, and that their accounts were operated by Mr Li. Mr Jiang said that he contacted Mr Li through Liu Yadong of the Jiangsu Yue Da Group Company Limited in order to tell him that the shares held in the two accounts had been acquired by Nanjing Zhongxinyue. Mr Jiang, however, did not require the shares to be transferred into an account in the name of Nanjing Zhongxinyue or to be sold and the cash paid over. According to Mr Jiang, with the consent of the board of directors, it was agreed that any dealings in the

[22] Mr Wu could never be contacted by the SFC.

shares would remain the responsibility of Mr Li who would act in conjunction with Nanjing Zhongxinyue.

113. Mr Jiang went on to say that at that time Jiangsu Yue Da South Holding Company Limited, one of the shareholders of Nanjing Zhongxinyue - and seemingly a member of the Jiangsu Group - was also indebted to Nanjing Zhongxinyue in respect of goods sold and delivered. The debt, he said, had been outstanding for some time.

114. As to the manner of the repayment of this debt, as Mr Jiang understood it, repayment was to be made by one of the companies in the Jiangsu Group. Although Mr Jiang did not hazard as to the identity of the company, the evidence shows of course that the largest flow of funds came from Yue Da Mining.

115. Mr Jiang said that it was further agreed that, as Nanjing Zhongxinyue was keen to invest in the Hong Kong share market, the repayment due to it would be diverted to Mr Li so that he could invest in the Hong Kong market on behalf of Nanjing Zhongxinyue, adding to the portfolio of Yue Da Mining shares already made over by Mr Wu. This arrangement, said Mr Jiang was put into effect.

116. A desire to acquire Yue Da Mining shares at a time of transformation is understandable. However, for a number of reasons to which we shall refer later in this report, Nanjing Zhongxinyue appears to have adopted a surprisingly lax approach to the entire arrangement, seemingly leaving matters almost solely

to Mr Li. The amounts of money involved were not insignificant: they ran into several million dollars. If the evidence is accepted, this was money paid to Nanjing Zhongxinyue and therefore its property. However, there is no evidence of any contemporaneous record of the agreement, no evidence of regular reports by Mr Li, no evidence of regular meetings to discuss the health of the portfolio. To all appearances, Mr Li was permitted (with the bare minimum of instruction or enquiry) to keep acquiring the single share over an extended period of time while that share's value diminished. It is as if Nanjing Zhongxinyue was entirely disinterested in the fate of its own investment. Either that all it had at some stage allied itself to an arrangement in which it did no more than lend its name to that arrangement enabling Mr Li to use the funds of the Jiangsu Group to acquire Yue Da Mining shares.

CHAPTER 3

THE LAW

117. The following directions of law were given by the Chairman to the Tribunal members. All determinations made in this report were made in accordance with these directions.

"Market Misconduct"

118. The Financial Secretary's Notice cited three forms of market misconduct, namely, false trading, price rigging and stock market manipulation. In this regard, section 245(1) of the Securities and Futures Ordinance, Chapter 571 ("the Ordinance") provides that:

> " '**Market misconduct'** means –
>
> (a) insider dealing;
>
> (b) false trading within the meaning of section 274;
>
> (c) price rigging within the meaning of section 275;
>
> …
>
> …
>
> (f) stock market manipulation within the meaning of section 278,
>
> and includes attempting to engage in, or assisting, counselling or procuring another person to engage in, any of the conduct referred to in paragraphs (a) to (f)."

119. The Ordinance goes further to include those persons who have "connived with" a perpetrator of market misconduct as also having engaged in market misconduct. In this regard, section 252 of the Ordinance provides that:

> " (4) Subject to subsections (5) and (6), the Tribunal may identify a person as having engaged in market misconduct pursuant to subsection (3)(b) if -

(a) he has perpetrated any conduct which constitutes the market misconduct;

(b) …

(c) notwithstanding that he has not perpetrated any conduct which constitutes the market misconduct –

(i) the Tribunal identifies any other person as having engaged in market misconduct… and

(ii) he assisted or connived with that person in the perpetration of any conduct which constitutes the market misconduct, with the knowledge that such conduct constitutes or might constitute market misconduct."

120. The expressions "assisted" and "connived with" as they arise in section 252(4)(c)(ii) are to be given their ordinary English meaning. The expression "assisted" requires no explanation. It is well-used and well understood. As for the expression "connived with", in its active sense it means to secretly cooperate with another in a wrongful act; in its passive sense, it means to feign ignorance or to fail to take measures to prevent the improper conduct thereby implying tacit encouragement or consent to the conduct.

"False Trading"

121. In so far as it is relevant to the enquiry, section 274(1) of the Ordinance provides that:

"False trading takes place when, in Hong Kong or elsewhere, a person does anything or causes anything to be done, with the intention that, or being reckless as to whether, it has, or is likely to have, the effect of creating a false or misleading appearance –

(a) of active trading in securities… traded on a relevant recognised market or by means of authorised automated trading services; or

(b) with respect to the market for, or the price for dealings in,

> securities… traded on a relevant recognised market or by means of authorised automated trading services."

122. To be found liable, a person must therefore intend to create a false or misleading appearance in respect of the market for a particular share or must be reckless as to whether it has, or is likely to have, that effect. As to "intent", in *HKSAR v Fu Kor Kuen Patrick*[23], the Court of Appeal held that the appropriate test was whether the person appreciated that the results of his act were virtually certain. As to what constitutes recklessness, in *Sin Kam Wah & Another v HKSAR*[24] (per Sir Anthony Mason NPJ) the Court of Final Appeal directed that:

> "… juries should be instructed that… it has to be shown that the defendant's state of mind was culpable in that he acted recklessly in respect of a circumstance if he was aware of a risk which did or would exist, or in respect of a result if he was aware of a risk that it would occur, and it was, in the circumstances known to him, unreasonable to take the risk."

123. As to the primary objective of the false trading provisions, in *Sin Kam Wah* the Court of Appeal held that it was directed at the fact of market manipulation itself, citing the observation of Sir Anthony Mason in *North v Marra Development Ltd*[25] that:

> "It is in the interests of the community that the market for securities should be real and genuine, free from manipulation. "

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[23] [2011] 1 HKLRD 655.

[24] (2005) 8 HKCFAR 192, at 210.

[25] [1981] 148 CLR 42, at 59.

124. In the same judgment, Sir Anthony Mason expressed himself more fully when he said:

> "It seems to me that the object of the section is to protect the market for securities against activities which will result in artificial or managed manipulation. The section seeks to ensure that the market reflects the forces of genuine supply and demand. By genuine supply and demand I exclude buyers and sellers whose transactions are undertaken for the sole or primary purpose of setting or maintaining the market price."

125. These observations were made by Sir Anthony Mason in construing section 70 of the Securities Industry Act 1970 (NSW) which spoke of "false trading and market rigging transactions". The Tribunal has proceeded on the basis that these observations are equally accurate when defining the essential purpose of the provisions of section 274 of the Ordinance.

"Price Rigging"

126. Insofar as it is relevant to the enquiry, section 275 of the Ordinance provides that:

> " (1) Price rigging takes place when, in Hong Kong or elsewhere, a person –
>
> (a) enters into or carries out, directly or indirectly, any transaction of sale or purchase of securities that does not involve a change in the beneficial ownership of those securities, which has the effect of maintaining, increasing, reducing, stabilising, or causing fluctuations in, the price of securities traded on a relevant recognised market or by means of authorised automated trading services; or
>
> (b) enters into or carries out, directly or indirectly, *any fictitious or artificial transaction or device*, with the intention that, or being reckless as to whether, it has the effect of maintaining, increasing, reducing, stabilising, or causing fluctuations in, the price of securities, or the price

for dealings in futures contracts, that are traded on a relevant recognised market or by means of authorised automated trading services.

(2) …

(3) For the purposes of subsections (1)(b) and 2(b), the fact that a transaction is, or at any time was, intended to have effect according to its terms is not conclusive in determining whether the transaction is, or was, not fictitious or artificial." [our emphasis]

127. In the context of the section, an "artificial transaction or device", connotes a transaction, tactic or ploy that, although made to look natural, is not, and whatever its outward appearance, does not reflect the interplay of genuine market forces. In that respect it is false or misleading.

128. The Tribunal accepted the submission by Mr Yeung, leading counsel for Yue Da Group (HK), that we must distinguish between legitimate trading strategies that are intended to anticipate and respond to prevailing market forces and those designed to manipulate prices and/or deceive purchasers and sellers. In the opinion of the Tribunal, in determining whether there has, by way of artifice, been an attempt by a person to undermine an open and free market in which the natural forces of supply and demand determine price, the true *intent* of that person (which includes recklessness on his part) must be ascertained.

"Stock Market Manipulation"

129. Insofar as it is relevant to the enquiry, section 278(1) of the Ordinance provides that:

" (1) Stock market manipulation takes place when, in Hong Kong or elsewhere -

(a) …

(b) …

(c) a person enters into or carries out, directly or indirectly, two or more transactions in securities of a corporation that by themselves or in conjunction with any other transaction maintain or stabilise, or are likely to maintain or stabilise, the price of any securities traded on a relevant recognised market or by means of authorised automated trading services, with the intention of inducing another person to sell, purchase or subscribe for, or to refrain from selling, purchasing or subscribing for, securities of the corporation or of a related corporation of the corporation."

The standard of proof

130. Section 252(7) of the Ordinance provides that:

"… the standard of proof required to determine any question or issue before the Tribunal shall be the standard of proof applicable to civil proceedings in a court of law."

131. That standard is the "balance of probabilities" In *Solicitor (24/7) v The Law Society of Hong Kong*[26], the Court of Final Appeal accepted the correctness of the approach to the civil standard of proof expressed by Lord Nicholls in *Re H & Others (Minors) (Sexual Abuse: Standard of Proof)*[27], namely that:

"The balance of probability standard means that a court is satisfied an event occurred if the court considers that, on the evidence, the occurrence of the event was more likely than not. When assessing the probabilities the court will have in mind as a factor, to whatever extent is appropriate in the particular case, that the more serious the allegation the less likely it is that the event occurred and, hence, the stronger should be the evidence before the court concludes that the allegation is established on the balance of probability."

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[26] [2008] 2 HKLRD 576.

[27] [1996] AC 563 at 586 D-G.

132. In the light of this, the Tribunal has reached its determinations on the basis that allegations of market misconduct are serious allegations affecting the reputation and good standing of individuals or corporations found to have conducted such misconduct.

Proof of the statutory defences

133. Section 274 of the Ordinance - the section on that sets out the elements of false trading - provides in subsection (6) that a person -

> "… shall not be regarded as having engaged in market misconduct by reason of false trading… if he establishes that the purpose for which he committed the act was not, or, where there was more than one purpose, the purposes for which he committed the act did not include, the purposes of creating a false or misleading appearance of active trading in securities, or with respect to the market for, or the price for dealings in, securities…"

134. Section 275 - the section that sets out the elements of price rigging - provides in subsection (4) a defence to the same effect, namely, that a person shall not be regarded as having engaged in price rigging if he establishes that the purpose for which the securities were sold or purchased did not include the purpose of creating a false or misleading appearance with respect to their price.

135. Both statutory defences look to "purpose", that is, to intent.

136. The burden imposed on a person seeking to invoke the statutory defences is the persuasive burden of proof, that is, the absence of the requisite purpose must be established on the balance of probabilities.

137. It is not obligatory for a specified person to produce evidence in order to establish the defences. In this regard, in *Braysich v R*,[28] French CJ said:

> "The legal burden on him was to prove on the balance of probabilities that he lacked the proscribed purpose. One way of doing that was to adduce or point to evidence inconsistent with the proposition that he had that purpose. He did not have to point to evidence of his actual purpose in order to invoke the defence. Any evidence that could support an inference that the appellant did not have the proscribed purpose was relevant to the statutory defence…"

The importance of identifying "the primary purpose"

138. Leaving aside for the moment the issue of recklessness, the identification of "intent" is integral to both proving and providing a defence to false trading, price rigging and stock market manipulation. As stated earlier, in attempting to identify intent the test to be employed is whether the person appreciated that the results of his act were virtually certain.

139. But a particular set of actions is not always occasioned by a single intention or purpose. The finder of fact (the Tribunal) may find that a particular set of actions took place for more than one reason, in other words that it was motivated by more than one purpose. If that is the case, it may be necessary to identify the primary purpose. In identifying a primary purpose, the Tribunal has been guided by the words of Lord Wilberforce in *Howard Smith Limited v Ampol Petroleum Limited*[29]:

> "… when a dispute arises whether directors of a company made a particular decision for one purpose or another, or whether, there being more than one purpose, one or another purpose was the substantial or primary purpose, the

[28] [2011] HCA 14, 276 ALR 451.

[29] [1974] AC 821, at page 831.

> court… is entitled to look at the situation objectively in order to estimate how critical or pressing, or substantial or, per contra, insubstantial an alleged requirement may have been. If it finds that a particular requirement, though real, was not urgent, or critical, at the relevant time, it may have reason to doubt, or discount, the assertions of individuals that they acted solely in order to deal with it, particularly when the action they took was unusual or even extreme."

140. In summary, intent may be determined by making a wider investigation and looking to all the surrounding circumstances. In this regard, see *Hindle v John Cotton Limited*, per Viscount Finlay[30]:

> "Where the question is one of abuse of powers, the state of mind of those who acted, and the motive on which they acted, are all important, and you may go into the question of what their intention was, collecting from the surrounding circumstances all the materials which genuinely throw light upon that question of the state of mind of the directors so as to show whether they were honestly acting in discharge of their powers in the interests of the company or were acting from some bye-motive, possibly of personal advantage, or for other reason."

Circumstantial evidence and the drawing of inferences

141. As is invariably the case in matters related to the investigation of possible market misconduct, the Tribunal in this present matter has been drawn to consider whether certain findings of fact may be inferred from the surrounding evidence. Inferences may be drawn but may only be drawn from proven facts; put another way, inferences must be properly grounded in the primary facts found. As it was expressed by Ribeiro PJ in his judgment in *Nina Kung v Wong Din Shin*[31]:

> "The court guards against indulging in conjecture under the guise of

[30] (1919) 56 Sc.L.R. 625, 630-631.

[31] (2005) 8 HKCFAR 387, at page 441.

> drawing an inference where the primary evidence does not logically and reasonably justify the particular inference in question."

142. As to the proper approach to the drawing of inferences, Sir Anthony Mason NPJ, in his judgment in the Court of Final Appeal in *HKSAR v Lee Ming Tee*[32], said:

> "… that conclusion was not to be reached by conjecture nor, as the respondent submitted, on a mere balance of probabilities. It was to be plainly established as a matter of inference from the proved facts."

Good character

143. The Tribunal bore in mind that a person of good character is less likely than otherwise might be the case to have committed the alleged misconduct and that good character supports his credibility in respect of both his evidence before the Tribunal and provided in records of interview, letters and other statements.

Lies

144. The Tribunal has been directed that a lie in itself does not prove that the maker of the lie is culpable of the misconduct alleged against him or her. People innocent of wrongdoing sometimes tell lies: perhaps as a misguided reaction to a problem or to postpone facing up to it or to attempt to deflect ill-founded suspicion or to fortify their defence. Even if the Tribunal is satisfied that a person has told untruths, either in oral testimony or in written evidence (such as interview statements or letters) it does not follow that his or her evidence must be rejected in its entirety. It is always open to the Tribunal to give due weight to parts of evidence placed before it and to reject other parts.

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[32] (2003) 6 HKCFAR 336.

Expert evidence

145. The Tribunal received the evidence of three expert witnesses: Mr Cheng Kai Sum, Mr Ermanno Pascutto and Mr John Lees. It received their evidence, containing both factual information and expressions of opinion, because it was likely to be outside the knowledge and experience of the Tribunal.

146. The Tribunal was directed that expert evidence went too far, and was to be ignored, if it sought to state the purpose or purposes for which the specified corporation's and persons in this enquiry acted, that is, if it sought to determine intent. In this regard, the following observations of the Court of Final Appeal in *Fu Kor Kuen Patrick & Others v HKSAR*[33] are pertinent:

> "… an expert in firearms may be able to give useful evidence in a case of homicide, but such evidence would not include an opinion as to whether the accused discharged a weapon with intent to kill. The legitimate evidence of the expert may be of relevance to the judgement of a judge or jury about the issue of intention, but any opinion of the expert on that point will almost certainly be based at least in part upon inferences of fact and matters of judgement outside his or her field of expertise. Similarly, an expert in the securities market may be able to give evidence which is relevant to a decision about the intention, or purpose, with which a trader acts. Such evidence may disclose information about conditions or forces in the market that would not otherwise be apparent to a tribunal of fact. It may throw light on possible influences or consequences of conduct. It may provide circumstantial material that is useful, perhaps necessary for a judgment about the state of mind with which a trader acted. However the witnesses in the present case went further than that. They gave their opinions about the purpose or purposes with which the appellants acted…"

[33] Unreported FACC 4/2011.

147. The Tribunal has been directed that it is not bound to accept the evidence of an expert witness in so far as it forms an expression of opinion. The Tribunal is entitled to accept or reject all or part of that evidence, coming to its own conclusions on such matters based on a consideration of all the evidence. The Tribunal is also in a position to prefer the evidence of one expert to another.

Separate consideration

148. The Tribunal has considered the case against and for each of the specified persons separately.

Attribution of liability to the corporations specified in the Financial Secretary's Notice

149. Two corporations have been specified in the Financial Secretary's Notice: Yue Da Mining and Yue Da Group (HK). However, as Viscount Haldane observed in *Lennard's Carrying Company v Asiatic Petroleum Ltd*[34]:

> "… a corporation is an abstraction. It has no mind of its own any more than a body of its own; its active and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the directing mind and will of the corporation, the very ego and centre of the personality of the corporation."

150. The acting and directing will of a corporation is not restricted however to a single person who may most accurately be described as the directing mind and will of the corporation. Not every act on behalf of a company, except perhaps a small family business, could be expected to be the result of a decision by the person who, for all practical purposes, is the proprietor. In larger

[34] [1915] AC 705, at 715.

companies there may be no such person; indeed, invariably there is not. Equally, not every act on behalf of the company could be expected to be the subject of a resolution of the board of directors or a unanimous decision of the shareholders. In *Meridian Global Funds Management Asia Limited and Securities Commission*[35], a judgment of the Privy Council, Lord Hoffmann spoke of the rules that deem a corporation to exist and the rules also that define what acts count as acts of that corporation; in short, what acts are to be attributed to the company. In this regard, having looked to the primary rules of attribution, he went on to say:

> "Not every act on behalf of the company could be expected to be the subject of a resolution of the board or a unanimous decision of the shareholders. The company therefore builds upon the primary rules of attribution by using general rules of attribution which are equally available to natural persons, namely, the principles of agency. It will appoint servants and agents whose acts, by a combination of the general principles of agency and the company's primary rules of attribution, count as the acts of the company, and having done so, it will also make itself subject to the general rules by which liability for the acts of others can be attributed to natural persons, such as estoppel or ostensible authority in contract and vicarious liability in tort."

151. As to the issue of vicarious liability in tort, the extent of this liability has been defined by Lord Nicholls in his speech in *Dubai Aluminium Co v Salaam*[36]:

> "Perhaps the best general answer is that the wrongful conduct must be so closely connected with the acts the partner or employee was authorised to do that, for the purpose of the liability of the firm or the employer to third parties, the wrongful conduct may fairly and properly be regarded as done by the partner while acting in the ordinary course of the firm's business or

[35] [1995] 2 AC 500, at 506.

[36] [2003] 1 BCLC 32, page 21.

> the employee's employment. Lord Millet said as much in *Lister v Hesley Hall Ltd* [2002] 1 AC 215, 245. So did Lord Steyn at pp 223-224 and 230."

152. Lord Nicholls went on to consider the liability of a corporation in circumstances in which an employee, while motivated by an intention to benefit the corporation, acted wrongfully or dishonestly. He said[37]:

> "Take a case where an employee does an act of a type for which he is employed but, perhaps through a misplaced excess of zeal, he does so dishonestly. He seeks to promote his employer's interests, in the sphere in which he is employed, but using dishonest means. Not surprisingly, the courts have held that in such a case the employer may be liable to the injured third party just as much as in the case where the employee acted negligently. Whether done negligently or dishonestly the wrongful act comprised a wrongful an unauthorised mode of doing an act authorised by the employer, in the oft repeated language of the 'Salmond' formulation: see Salmond on Torts, 1st ed, (1907), p83."

153. The "close connection" approach has been approved by the Court of Final Appeal in *Ming An Insurance Co (HK) Ltd v The Ritz-Carlton Ltd*[38]. In his judgment, Bokhary PJ concluded (paragraph 25):

> "For all the foregoing reasons, I regard close connection as the basic criterion for vicarious liability for all torts committed by an employee during an unauthorised course of conduct, whether intentional wrongdoing or mere inadvertence is involved. This is not to say that this criterion is to be treated like a statutory formula. Its application is always to be undertaken in context."

154. In considering the principle in context, it is important to recognise that an employer is not liable if the employee has embarked upon a "frolic of his

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[37] Page 43.

[38] [2002] HKCFAR.

own". In such circumstances it cannot be said that the acts of the employee can rightly be regarded as modes, albeit improper modes, of carrying out his authorised activities. In this regard, Lord Wilberforce, in *Kooragang Investments Pty Ltd v Richardson &Wrench Ltd*,[39] said:

> "… The underlying principle remains that a servant, even while performing acts of the class which he was authorised, or employed, to do, may so clearly depart from the scope of his employment that his master will not be liable for his wrongful acts."

[39] [1982] AC 462, 473-475.

CHAPTER 4

A FAIR HEARING

155. One of the difficulties that clearly vexed the orderly progress of the SFC investigation in this matter was the difficulty in gaining access to and being able to interview all relevant parties including those who it was suspected would be named as specified persons and those, not necessarily suspected of any involvement in market misconduct, whose evidence would be relevant to the enquiry.

156. The practical difficulty facing the SFC was occasioned by the disbursement to various parts of the Mainland of many of the persons sought to be interviewed.

157. As we have indicated earlier, Mr Li, one of the specified persons in the Financial Secretary's Notice, although he gave a statement on the Mainland to the SFC, did not testify at the hearing either in person or by way of video link. In the end he refused any further involvement on the basis of his deteriorating health. No medical report was tendered as to his inability to assist the enquiry.

158. It appears that Mr Qian, another specified person, could not be located to be interviewed by the SFC. In addition, when documents were posted to his address, delivery was refused. On the evidence, Mr Qian refused to be engaged in the enquiry. Without equivocation, he took advantage of the fact that he resided outside of the Hong Kong jurisdiction.

159. In addition, witnesses of lesser importance could not be tracked down, one example being a man named Wu Guoyi, an apparent friend of Mr Li and a businessman whose evidence may perhaps have been of considerable importance.

160. A number of issues arise out of these difficulties.

161. The first is whether, having not given testimony before us, the two specified persons, Mr Li and Mr Qian, are capable of being identified as having engaged in market misconduct.

162. In this regard, section 252(6) of the Ordinance directs that the Tribunal shall not identify a person as having engaged in market misconduct… *without first giving the person a reasonable opportunity of being heard.* [our emphasis]

163. What constitutes a "reasonable opportunity" is to be determined in accordance with the circumstances of each case.

164. Looking first to Mr Li, he was given an opportunity to answer allegations of market misconduct during the course of the SFC investigation and took advantage of that, giving a detailed statement. After the Tribunal had been constituted and he had been named as a specified person, Mr Li was served with all relevant documents. Indeed, a directions hearing held on 22 May 2012 was adjourned because, among other reasons, Mr Li had only received the relevant documents the day before the hearing and had been unable to make arrangements to come to Hong Kong. As it was, shortly thereafter Mr Li, who,

as we have said, complained of very poor health, said that he was too ill to come to Hong Kong to give evidence but agreed to do so via video link from near his home in the Mainland. Arrangements were then put in place to set up the video link. As it was, however, by email dated 2 July 2013 Mr Li said that, as his health had deteriorated further, he was forced to travel to Shanghai for further medical treatment and could play no further role in the proceedings. Some four days later he sent a lengthy letter. That letter, in the main, was a plea to have no further involvement in the proceedings but also touched upon the subject matter of this enquiry.

165. With respect to Mr Li, as we have said earlier, at no time did he supply any form of independent written evidence of the nature and extent of his health problems. If we had received such evidence, and if that evidence had made it plain that Mr Li was in no position to protect his own interests, our position may have been different.

166. It is also pertinent to note that his communications in early July 2013 - received by us after the hearing had commenced and he had been given notice that he would shortly be called upon to testify - constituted notice that he did not wish to be troubled any further. In short, for all practical purposes he washed his hands of the enquiry. He did not ask for an adjournment so that he could have his medical treatment and then return to give evidence.

167. In such circumstances, having regard to the full history of the matter, we are satisfied of two things. First, Mr Li was given a reasonable opportunity of being heard. Second, on the evidence available to us, that opportunity was

not undermined by the fact that Mr Li's sickness prevented him in any way, either by way of oral evidence or by way of a further written statement, from being heard.

168. In respect of Mr Qian, all relevant documents were posted to his address in the Mainland but he refused to accept delivery. Even though it was acknowledged that it was probably a futile exercise, further documents generated in the process of the enquiry were posted to him to keep him informed. The Ordinance requires that a specified person be given the opportunity to be heard, it does not require that he should take up the opportunity. Taking into account that Mr Qian was at all times outside of the jurisdiction, we are satisfied that nothing further could reasonably have been done to provide Mr Qian with the opportunity of being heard.

169. In respect of both Mr Li and Mr Qian, we are therefore satisfied that it is open to us, should the evidence support such a finding, to find that either or both of them engaged in one or more forms of market misconduct.

170. As to the nature of the evidence that we may consider, it is now settled that this Tribunal conducts proceedings of an inquisitorial nature. In furtherance of this responsibility, the Ordinance gives to the Tribunal the power to consider a broad range of evidential material. Section 253(1) provides -

> " (1) Subject to the provisions of Schedule 9 and any rules made by the Chief Justice under section 269, the Tribunal, for the purpose of any proceedings instituted under section 252, may, on its own motion or on the application of any party before it -
>
> (a) receive and consider any material by way of oral evidence,

> written statements or documents, even if the material would not be admissible in evidence in civil or criminal proceedings in a court of law."

171. Written statements and miscellaneous documents may therefore be received and considered by us even if such material would not be admissible in evidence in civil or criminal proceedings in a court of law. It is not necessary, therefore, for a person to give oral testimony before his evidence - placed before the Tribunal in some other form, for example, by way of a written statement or similar document - is permitted to be considered.

172. That being said, it is fundamental that inquisitorial proceedings before the Tribunal must be fair. It has been said on numerous occasions that fairness does not operate in a vacuum. What is required of a fair hearing will vary from case to case.

173. It is patent of course that any person or corporate body specified in the Notice of the Financial Secretary should not be left in the dark as to the risk of prejudicial findings being made against them and thereby deprived of the opportunity to produce additional material of probative value.[40] Both Mr Li and Mr Qian were presented with all relevant materials and were able, if they wished, to produce additional material of probative value, for example, further statements and other supporting documents. The fact that Mr Qian (apparently)

[40] See the judgment of the Privy Council in *Mahon v Air New Zealand Ltd* [1984] 1 AC 808, more particularly the following citation at 821: "… any person represented at the enquiry who will be adversely affected by the decision to make the finding should not be left in the dark as to the risk of the finding being made and thus deprived of any opportunity to adduce additional material of probative value which, had it been placed before the decision maker, *might* have deterred him from making the finding even though it cannot be predicted that it would inevitably have had the result."

chose not to consider the relevant materials at all was his decision. As we have said earlier, he was given the opportunity to do so and, in light of that opportunity, to provide additional material of probative value if he wished.

174. Fairness has also dictated that we be aware of the fact that the reputations (and perhaps on-going careers) of the specified persons may be adversely affected by our determinations. Equally, the corporate reputations of the specified bodies - especially that of Yue Da Mining, a company listed on the Hong Kong Exchange - may be damaged by our determinations.

175. We have further taken into account that parties represented at the hearing may have wished to rely on certain evidence (such as interview records or letters) not supported by oral testimony given during the course of the hearing or, to the contrary, may have wished us to give such evidence no weight.[41]

176. Each of our determinations has been reached in the context of whether the interests of fairness permits them to be made.

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[41] In this regard, for example, counsel representing Yue Da Group (HK) sought to place reliance on the evidence of Mr Li. In his closing submissions, Mr Keith Yeung SC, leading counsel for that company, said the following: "Li's evidence is important. He was personally involved in the transactions in question. He had personal knowledge of the events leading to those transactions. His mental status and intention may determine whether the transactions he undertook were innocent or culpable market misconduct. At the time Yue Da Group (HK) had three directors. One of them (Chairman Hu) has died. The other one (Gao) has never been involved. Li is the only director who is in the position to explain the reasons behind those transactions done for and in the name of Yue Da Group (HK). His evidence is… consistent with the other objective circumstantial evidence. It is submitted that the notion of fairness (procedural and substantive) which underpins the Tribunal procedure… requires that Li's evidence should be given full weight."

CHAPTER 5

YUE DA MINING'S REPURCHASE OF SHARES

177. Yue Da Mining's repurchase exercise was short. It ran for a period of five trading days from 16 January to 23 January 2008. In this short period, the company's repurchases amounted to 69.85% of the total market purchases (excluding non-AMS activities). A total of 58 buy orders were placed resulting in a repurchase of 862,000 shares at a cost of HK$4,912,042.68.

178. Concurrently with this, Mr Li was actively trading in Yue Da Mining shares through the HSBC account of Zhang Hongyan. In this regard, between 3 December 2007 and 13 February 2008, he purchased a total of 1,388,000 Yue Da Mining shares, sold 680,000 shares and was left with a credit of 708,000 shares. The trading was regular too, taking place on 36 out of 42 trading days.[42]

179. In addition, of course, Yue Da Group (HK), with Mr Li at the helm, was actively purchasing Yue Da Mining shares. In December 2007 it had purchased 451,000 shares at a cost of HK$3,046,099.17 while in January 2008 it purchased a further 284,000 shares at a cost of HK$1,799,555.53.

180. There was therefore active trading in the shares of Yue Da Mining by Mr Li (personally) and by him (in his capacity as a director of and responsible

[42] Mr Li began trading in the HSBC account of Su Linian in early January 2008 but his purchases were minimal until late in February when the bulk of the trading in this account began to take place.

officer for Yue Da Group (HK)) at and about the time of the share buy-back exercise.

181. In this regard it is to be remembered that Yue Da Mining and Yue Da Group (HK) shared offices throughout this time and that Mr Li, although not a director of Yue Da Mining, was a director of its controlling shareholder, Yue Da Group (HK), and possessed signing powers on behalf of the company.

182. Despite this trading which, whether intended or unintended, must have had the effect in the eyes of the market of putting the repurchase exercise in the context of broader active trading, the price of Yue Da Mining shares declined during the repurchase exercise. On the opening day of the repurchase exercise, Yue Da Mining shares closed at HK$6.00. On 23 January, the last day of the repurchasing exercise, they closed the day at HK$5.40. This constituted a decline in the share price over that limited period of 60 cents. Over the same period, the Hang Seng Index declined from 24,450 to 24,090.

183. What then was the purpose of the repurchase exercise? Was it, as appearances may suggest, part of a broader scheme to support the share price of Yue Da Mining at a critical period in its corporate history, another battery of artillery to add to the coordinated firepower? Or was it an independent, unconnected action?

184. Mr Dong, the CEO of Yue Da Mining, testified that the share repurchase exercise was his idea. At the time he proposed the repurchase, he said, and during its short duration, he had no idea that Mr Li was using HSBC

"nominee" accounts to deal in Yue Da Mining shares and had no idea that Yue Da Group (HK) was also purchasing the shares. The fact that Yue Da Group (HK) had been acquiring further Yue Da Mining shares only came to his knowledge when reports were put before him in the ordinary course of events as to the acquisition of shares by major shareholders.

185. In short, if Mr Dong is to be believed, the share repurchase exercise - to his knowledge at least - was not part of some grander scheme to stabilize the price of Yue Da Mining shares. He did not connive with Mr Li, Mr Qian or Yue Da Group (HK) in any such scheme. The share repurchase exercise was instead an independent exercise to communicate confidence to investors, an exercise permitted by Hong Kong's prescriptive regime.

186. Mr Brewer, counsel for Mr Dong and Yue Da Mining, submitted (correctly, in our view) that two issues therefore presented themselves:

- The primary issue was whether the share repurchase exercise conducted through the market to communicate confidence in Yue Da Mining's shares was in itself manipulative and therefore a form of market misconduct.
- The secondary issue was whether Mr Dong, acting in his capacity as CEO of Yue Da Mining, assisted or connived with Mr Li and/or Mr Qian in any misconduct of which they may have culpable arising out of their dealings in Yue Da Mining shares.

187. In this chapter, we shall look to what Mr Brewer described as the primary issue, namely, whether the share repurchase exercise, conducted openly through the market, constituted of itself a form of market misconduct.

Mr Dong's evidence as to the purpose of the repurchase

188. As to how it was that the share repurchase exercise came about, Mr Dong provided a comprehensive statement prepared in conjunction with his legal representatives. In addition, of course, he testified before the Tribunal. His evidence may be summarized as follows.

189. On Saturday, 12 January 2008, Mr Dong communicated with Mr Hu expressing his concern that, although the business of Yue Da Mining has been transformed, this had not been fully appreciated by the market. Mr Dong believed that a fair valuation should be HK$9.00 per share. The share price however remained undervalued. In this regard, Mr Dong testified that in October 2007 the Kingsway Group's Liber Research Team had recommended a target price of over HK$8.00 per share but the price had drifted to downwards from HK$6.77 on 31 December 2007 to HK$6.65 on 11 January 2008 with a further fall to HK$5.00 on 14 January 2008. Mr Dong said that he recommended that a sum of up to HK$10 million be employed to repurchase Yue Da Mining shares, the price to be under HK$7.00 per share.[43]

[43] The communication ended as follows: "For this reason, we recommend the Company to consider share repurchase under the current market conditions. If this is feasible, it is recommended that the repurchase price be limited to under $7.00 and the amount of funds for the repurchase should not exceed of $10 million. Kindly indicate whether the above recommendation is proper."

190. The proposal to undertake a share repurchase exercise was approved, Mr Dong being instructed to "proceed in accordance with the relevant regulations".

191. As to the authority to undertake a repurchase, on 27 June 2007 Yue Da Mining had its annual repurchase mandate renewed at a shareholders meeting, the mandate permitting it to repurchase up to 10% of the company's issue share capital: calculated at the date of that meeting or 25,955,800 shares.

192. According to Mr Dong, he requested Mr Qian to proceed with the repurchase exercise. His instructions, he said, were not to purchase too many shares in a single day lest it cause a significant increase in (as opposed to mere support for) the share price and raise the cost of repurchase. He said that he further instructed that a sum of up to HK$2 million was to be used on any given day and that the repurchases were all to be reported in accordance with the Listing Rules.[44]

193. As we have said, the repurchase exercise ran for a period of five trading days. This was from the afternoon of 16 January until 23 January 2008. The exercise then ceased, this despite the fact that less than 50% of the HK$10 million set aside for the exercise had been expended.

194. As to why the exercise came to such an abrupt halt, Mr Dong said that it was occasioned by the confluence of two events: first, the urgent need to raise

[44] The methodology of the trading will be looked at in the next chapter.

a sum of HK$100 million and, second, the fortuitous approach of the finance company, SBI-E2 Capital, with the advice that a further share placement was now a feasible option.

195. As to the need to urgently raise a sum of HK$100 million, Mr Dong's evidence was to the following effect.

196. The Hong Ling Project (one of the major mining acquisitions) had been purchased from the Balin Zuo Qi Peoples' Government which, after the successful bid, had approached the Jiangsu Group and Yue Da Mining for an early payment of a deposit so that it could be seen to meet its local target in attracting outside investment. It backed up this request with a commercial quid pro quo, details of which are somewhat complex and need not be described. What matters is that the deposit sought, and agreed to by the Jiangsu Group and Yue Da Mining, was HK$100 million. The payment of the deposit however was dependent on the formal approval of the vehicle that would reflect the 80% interest of the Jiangsu Group and Yue Da Mining in the Hong Ling Project. According to Mr Dong, it was very much doubted that this could be achieved before the Lunar New Year in February 2008.[45]

197. As it was, however, on 23 January 2008 Mr Hu, the Chairman of the Jiangsu Group, was informed by the Balin Zuo Qi Peoples' Government that a certificate of approval had now been issued and that it was anxious to receive the HK$100 million deposit by the end of the month.

[45] The vehicle was described by Mr Dong as a "30-year Sino-Foreign Co-operative Joint Equity Enterprise".

198. As to the fortuitous approach by SBI-E2 Capital, Mr Dong's evidence was to the following effect.

199. Following Yue Da Mining's November announcement of its acquisition of the Inner Mongolia mining rights (the Weng Qi and Hong Ling projects), he had been approached by a number of financial institutions eager to work with the Company to raise further capital by way, for example, of a further share placement. One of the companies which had shown particular interest was SBI-E2 Capital. In this regard, Mr Dong said that he had met two members of the company, Ms Christine Zheng Juan and Ms Vivian Ip Hung, in December 2007 and that they had visited the company in early January 2008. At that time however he stressed that a further placement exercise was unlikely, especially having regard to the sluggish condition of the market, and, even if it was contemplated, having regard to the very large sums of money required to finance the Inner Mongolia acquisitions, a share placement could only constitute a minor part of any capital raising exercise.

200. Mr Dong testified that, as it happened, however, on the evening of 23 January 2008, when he was still digesting the news that a sum of HK$100 million had to be raised without delay to pay the Balin Zuo Qi Peoples' Government, he was contacted by Ms Vivian Ip Hung of SBI-E2 Capital, her essential pitch being that, as the market was stabilising, she believed it would be possible for Yue Da Mining to conduct a further placement exercise with the shares priced at between HK$5.20 and HK$5.40.

201. Mr Dong said that he immediately reported the approach to Mr Hu, obtaining his approval to raise the deposit of HK$100 million by way of a further placement of 20 million shares but on this occasion with no discount.

202. In light of these instructions, Mr Dong said that he informed Ms Ip that the Company was interested in a second top-up placing exercise of 20 million shares but at a price of HK$5.40 per share or better. Later that evening, Ms Ip replied saying that there was sufficient interest to enable the placing exercise to go ahead.

203. According to Mr Dong, that same evening he gave instructions to Mr Qian to cease further share repurchases and instead to prepare for the placement exercise. The following day, he said, he instructed the company's solicitors to make submissions to the Stock Exchange in respect of the intended placement exercise.

204. In summary, the repurchase of shares ended prematurely because of the unexpected need to raise some HK$100 million in respect of the Inner Mongolia mining acquisitions and to do so before the end of that current month, that is, within a matter of a week or so. Equally importantly, the persistence of SBI-E2 Capital in pitching for business presented an almost immediate means of raising that sum.

205. According to Mr Dong, therefore, the share repurchase exercise was not a device to create a beneficial climate for the second share placement.

When the share repurchase exercise was decided upon no further share placement was in contemplation.

Considering evidence in support of Mr Dong's version of events

206. The coming together of unexpected events do happen of course, especially when a company is in the process of transformation. Nevertheless, the unexpected events described by Mr Dong (which occurred in the space of a few hours on the late afternoon and evening of 23 January 2008) require careful, if not sceptical consideration.

207. In our view, there is however evidence to support Mr Dong's version of events.

208. As Yue Da Mining was seeking, within a period of 30 days after repurchasing its own shares, to issue new shares by way of a top-up placement, the permission of the Stock Exchange was required. It is the correspondence with the Stock Exchange by Yue Da Mining's solicitors which provides contemporaneous support for Mr Dong's version of events.

209. A letter of 25 January 2008 forms part of the correspondence. In that letter, Messrs Chiu & Partners explain why the top-up placement exercise is so suddenly required, doing so with specific reference to the earlier than expected certificate of approval and the consequent need to raise the HK$100 million.

210. Any implied suggestion that the Company had repurchased its shares at a relatively high price while proposing to now place its shares at a relatively low price was also sought to be dispelled.[46]

211. In simple terms, what this evidence dispels is any suggestion of recent invention on the part of Mr Dong. Within some 48 hours of the events which he described taking place on 23 January 2008, those same events are being referred to - that is, the events giving rise to the need to raise an urgent deposit - in formal correspondence with the Stock Exchange.

212. Support for Mr Dong's evidence is also to be found in the testimony of Ms Vivian Ip Hung. During the course of her testimony she accepted that it had been she and her colleagues who had broached the matter of a further share placement. She accepted that Mr Dong was (at best) equivocal about a further placement exercise; indeed, she accepted the word "sceptical" as accurately describing how he felt at the time.[47] She further accepted that she took the initiative to contact Mr Dong on the evening of 23 January 2008, doing so in

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[46] In this respect, the letter states: "As the Exchange may have noted, the placing price is the same as the closing price of the shares on 23 January 2008 and no discount has been given. By reference to the December 2007 placing, more than 16% discount (from the then closing price of the last trading day before the date of the announcement of the December 2007 placing) was given for the then closing price. If such discount rate is to be adopted, the market price would have to reach as high as approximately $6.43 for the share to be placed at a placing price of $5.40 per share. All the shares repurchased under the repurchase transactions were at a lower price than that. As such the Company does not consider that the shares were repurchased at a relatively high price or are proposed to be placed at a relatively low price."

[47] The following is an extract from her evidence –

"Q. And, when, in December, you talked about the placement, it's correct to say that you were talking in terms of possibilities only?
A. Yes, of course.
Q. You were pursuing possible business opportunities for SBI-E2 Capital?
A. Correct.
Q. And, on 23 January, the initiative to suggest that a particular placement be done was your initiative, yes?
A. Correct."

order to tell him that, in her opinion, "the macro market was relatively stable and there was a window of opportunity… to do the share placement."[48] It was that same evening, she said, that the share placement agreement was agreed. Mr Dong was dissatisfied with the price range that she had suggested (something being said to the effect that the parent company was also unhappy at that range) and insisted that the placement would have to proceed at a price of HK$5.40.[49]

213. The contemporaneous evidence provided by the correspondence with the Stock Exchange, in dispelling any suggestion of recent invention, adds to the inherent credibility of Mr Dong's version of what happened. The evidence of Ms Ip, in giving third party support to that version, adds to its inherent credibility.

214. We would add that, in our judgment, Mr Dong gave convincing evidence in respect of these matters as did Ms Ip. We had no reason to doubt either of them.

Analysis of the repurchase dealing

215. During the course of the hearing considerable time was spent examining the nature and extent of the share dealing that took place not only in respect of the repurchase but in respect of all other dealing exercises too.

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[48] Ms Ip said that, in her experience, a "window of opportunity" was not determined solely by price but by having regard to a host of other factors that in her lengthy experience of managing placements were relevant.

[49] HK$5.40 was the closing price of the previous day's trading.

216. In our view, the analysis of the share dealing related to the repurchase was of only limited assistance.

217. All the trading was conducted through Yue Da Mining's BOCI securities account. There is no evidence that Mr Dong placed any orders. Based on the evidence presented to us, the instructions to BOCI were given by Mr Qian only.

218. In the five days of trading Mr Qian placed a total of 58 buy orders. None of the orders were placed at or below the prevailing best bid price. Of the 58 buy orders, 51 had an order price high than the current "best ask" price. Clearly, in the context of a thinly traded market, the intent was to show support for the shares by way of the prices offered.

219. In our view, however, this does not tell against Mr Dong's evidence concerning the purpose of the repurchase exercise. The purpose, he testified, was not to create a short term boost in the share price but to show solid support for it.

220. Even if it could be demonstrated that Mr Qian did not remain entirely within the boundaries of his instructions, it does not follow that Mr Dong was aware of this and approved.

Our findings as to the purpose of the repurchase exercise

221. We are therefore prepared to accept that the share repurchase exercise was not initiated in order to create a benign climate for the second share

placement exercise. That, however, still leave the question: having regard to the stated purpose for the exercise given by Mr Dong (which we accept) was the exercise in itself a permitted one?

The evidence of Mr Pascutto

222. In considering this issue, we were substantially assisted by the testimony of Mr Ermanno Pascutto given by way of video link from Canada. In his capacity as an expert, Mr Pascutto was, we think, eminently suited to explain how it was that the current Hong Kong regulatory regime came into being:

i. Between 1981 and 1983, he was Director of the Market Policy Division at the Toronto Stock Exchange during which time he developed the first share repurchase rules for share repurchases (referred to in Canada as "normal course issuer bids") through the facilities of the Toronto Stock Exchange.

ii. Between 1984 and 1989, he was Executive Director of the Ontario Securities Commission, one of his responsibilities being oversight of the Toronto Exchange's share repurchase rules.

iii. Between 1989 and 1994, he was Executive Director, Corporate Finance, of the then newly established SFC in Hong Kong. As such, he was responsible for oversight of the listing functions of the Hong Kong Stock Exchange.

223. As to his time with the SFC in Hong Kong, Mr Pascutto said:

> "I worked with the Exchange on the development and administration of the Listing Rules including the introduction to Hong Kong of the new share

> repurchases rules in chapter 10 of the Listing Rules. I was also responsible for the development and administration of the SFC's Code on Takeovers and Mergers and the development of a new Code on Share Repurchases."

224. As Mr Pascutto set out in his report, until 1991 Hong Kong companies were generally not permitted to purchase their own shares. As such there were neither rules of the Stock Exchange nor codes of the SFC that governed share repurchases. However, following the worldwide stock market crash of October 1987, a far-reaching review of the operation and regulation of the Hong Kong securities industry took place. The Securities Review Committee in its report of May 1988 recommended a number of structural reforms including the setting up of the SFC and the introduction of rules permitting Hong Kong companies to purchase their own shares. The SFC was established in 1989 and in 1991 - with the passage of the Companies (Amendment) Ordinance, amended Listing Rules and the publication by the SFC of a Code on Share Repurchases - listed companies were now able to buy-back their own shares.

225. As to the principal purposes of share repurchasing, Mr Pascutto said that there are a number of accepted purposes[50], among them being the following three:

i. to support the market price of shares particularly during periods of volatility, whether of markets in general or affecting the company in particular;

ii. to support the share price when there is a major seller in the market, and

[50] Taken from the February 2004 report on 'Stock Repurchase Programmes' by the Technical Committee of the International Organisation of Securities Commissions (the IOSCO Report).

iii. to signal to the market that management believes that the company's shares are undervalued or [to signal] management's optimism in the company's prospects.

226. If the stabilisation of a share price is a permitted purpose for a repurchase exercise - and Mr Pascutto was in no doubt that the Hong Kong regulatory regime, within prescriptive limits, permits the repurchase of shares for this purpose - it follows that repurchases by listed companies for this permitted purpose will inevitably have an influence on both the trading price and the volume of trading of a company's shares.[51]

227. This raises a number of regulatory concerns. As Mr Pascutto expressed it, these concerns relate, first, to the fair treatment of shareholders; second, to ensuring an orderly market and, third, to ensuring the integrity of the market.

228. How are these concerns dealt with? In a prescriptive regulatory regime (such as Hong Kong, Canada and the United Kingdom) these concerns are met by imposing a coherent system of mandatory restrictions.

229. The protection of shareholders is generally addressed by way of requirements for shareholder approval, public disclosure and financial

[51] in this respect, the IOSCO Report (page 12) states: "The operation of SRPs inevitably has implications for companies' share prices and secondary market trading in their shares. The potential impact of open market SRPs on both volumes and share price could be significant and could extend over a considerable period."

restrictions which protect against jeopardising the financial solvency of a company.

230. The functioning of an orderly market is generally ensured by provisions which limit the effect of share repurchases, for example, by placing limits on the quantity of shares that may be repurchased in the market or the price that may be paid.

231. The integrity of the market is generally addressed by prohibiting a company from repurchasing its shares when the company has knowledge of price sensitive information that is not been publicly disclosed - this being one of the matters that falls for our consideration in this report.

232. If, subject to the constraints of Hong Kong's regulatory regime, share repurchases are permitted for the purpose of stabilising a listed company's share price, almost by definition what is permitted is an interference by the listed company in the free workings of the market in respect of its shares: in short, a form of market manipulation.

233. In this regard, Mr Pascutto made reference to the Securities and Futures (Price Stabilising) Rules, particularly to sections 4 and 5[52] which exempt stabilising action made in compliance with the Rules from being

[52] S.4 reads: "For the purpose of section 282(1) of the Ordinance, any stabilising action in respect of any relevant securities taken in compliance with these Rules shall not be regarded as constituting market misconduct." S.5 reads: "For the purposes of section 306(1) of the Ordinance, any stabilising action in respect of any relevant securities taken in compliance with these Rules shall not be regarded as constituting an offence under Part XIV (other than section 300 or 302) of the Ordinance."

regarded as market misconduct. "These Rules", he said, "make explicit in respect of price stabilisation that which, in my view, is implicit in the share repurchase rules i.e. that share repurchases made in compliance with the requirements of the Listing Rules and the Share Repurchase Code do not constitute share price manipulation or market misconduct."

234. Mr Pascutto further made reference to Rule 10.06(3) of Chapter 10 of the Listing Rules[53] which directs that a listed company is not permitted to issue new shares within 30 days of a share repurchase exercise without the approval of the Stock Exchange. The 30 day restriction, he commented, is in recognition of the fact that share repurchases are likely to have some effect on the market price. The 30 day restriction period gives the market a cooling off period so that the market price of the share is no longer influenced by the earlier share repurchase programme.

235. Elsewhere in his report, Mr Pascutto gave evidence of the fact that permitted share repurchase programmes in other jurisdictions also recognise that such programmes will inevitably have an effect on a listed company's share price and the volume of trade in respect of those shares.

236. By way of conclusion, Mr Pascutto said that, in his opinion -

> "Hong Kong's prescriptive regime regulating share repurchases was introduced on the understanding that permitted share repurchases by listed companies would inevitably have an effect on share prices and would tend to support such prices during periods of stress for the market in general or

[53] The Rule states that "An issuer whose primary listing is on the Exchange may not make a new issue of shares or announce a proposed new issue of shares for a period of 30 days after any purchase by it of shares, whether on the Exchange or otherwise (other than an issue of securities pursuant to the exercise of warrants, share options or similar instruments requiring the issuer to issue securities, which were outstanding prior to that purchase of its own securities), without the prior approval of the Exchange."

> for the shares of an individual company in particular. Indeed, it was accepted by the Hong Kong Government, LegCo, the regulators and the market that share price support during periods of market crisis or when a specific stock experienced a crisis was a good thing."

237. Share repurchases made in compliance with the prescriptive requirements of the Listing Rules and the share repurchase Code were considered to be in compliance with these regulatory requirements and therefore did not constitute market manipulation even if the repurchases, as is inevitably the case, supported or increased the share price.

Our conclusions in respect of Mr Pascutto's evidence

238. Mr Pascutto's evidence was considered and, in a number of respects, disputed by the SFC expert, Mr Cheng Kai Sum, Eric.[54]

239. As the presenting officer, Mr Kwan expressed it, the principal difference between them related to how the two of them viewed the nature and purpose of the Hong Kong regulatory regime. In the view of Mr Kwan, Mr Pascutto believed that, as long as the share repurchase rules were met (and the Yue Da Mining repurchase did) then there could not be market manipulation as

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[54] It is to be noted that counsel representing specified persons raised a number of objections to Mr Cheng's evidence being received by the Tribunal. Four objections in particular were as follow –

i. That Mr Cheng, as an expert, was not independent and impartial, his first opinion having been given when he was a senior officer with the SFC;
ii. That he had failed to consider how regulatory concerns in respect of market manipulation are dealt with (and answered) by the share repurchase code and listing rules;
iii. That he drew inferences from share trading patterns, that being a matter for the Tribunal; and
iv. That he attempted to explain and give a rationale to commercial activities, a matter outside of his expertise and in any event speculative.

These were all matters that we took into account in reaching our determinations in this report. However, having heard Mr Cheng give evidence, we were satisfied that his evidence should not be refused on the basis of his asserted lack of impartiality. We were further of the view that, Mr Cheng being an acknowledged expert in the securities market, certain of his analyses fell into his area of expertise and fell for consideration. That being said, under the guidance of the Chairman as to matters of law, care was always taken to recognize the limits to which Mr Cheng's evidence could legitimately be of assistance.

there would be no false or misleading appearance as to price and volume. In respect of the principal thrust of Mr Cheng's evidence, however, Mr Kwan was of the view that compliance with the regulatory regime was, of itself, not sufficient. What had to be considered was whether there was the presence of an "ulterior motive" which undermined the regularity of the repurchase.

240. As we have indicated earlier in this report, we were impressed by the expert evidence of Mr Pascutto. It was evidence given by a man with long experience of both constructing and operating stock market regulatory regimes. It was clearly stated and moved logically to a rational conclusion. We are satisfied that Mr Pascutto's opinion as to the true nature and extent of the regime governing repurchase of shares by listed companies is the correct one. As to the same issue, we found Mr Cheng's evidence less easy to follow, in parts perhaps too dense and forensic. That being said, at the end of the day, we did not find that there was a great deal of difference between them.

241. We are satisfied that - considered in isolation - if a listed company complies with all the prescriptive rules, it may lawfully repurchase its shares in order to maintain or support their price even though such action may distort the price which would otherwise obtain as a result of the natural supply and demand of the market. As Mr Pascutto put it, that is because the prescriptive regime itself protects the market and the exercise has been conducted within the terms of that regime. That, in our view, is a clear, easily understood interpretation that meets the purpose of the regulatory regime.

242. However, as Mr Pascutto made plain, he was looking to a repurchase exercise in isolation. It was not part of his mandate to look to broader issues such as a repurchase exercise that takes place when senior management are in possession of price sensitive information or, as is the assertion in the present case, when senior management have planned the exercise to be part of a broader strategy to undermine the market.

243. In our judgment, therefore, a repurchase exercise undertaken in isolation, that is, unaffected by the putting into effect of any complementary strategy, is lawful whatever the private intentions of senior management might be provided only that the terms of the governing prescriptive regime are fully met.

244. If however the repurchase exercise is part of a broader scheme that constitutes market misconduct and is intended to be such then, in our view, it is capable of constituting market misconduct even though in respect of the share repurchase itself, all the prescriptive terms have been met.

245. As we have already indicated, we are satisfied that the share repurchase exercise was not put into effect by Mr Dong to create a benign climate for the second share placement; in short, it was not put into effect when he was, in respect of the second share placement, in possession of price sensitive information.

246. That however still leaves to be answered what Mr Brewer described as the secondary issue, namely whether Mr Dong, when he launched the share

repurchase exercise, did so in the knowledge that Mr Li and/or Mr Qian were conducting a complementary set of exercises to acquire Yue Da Mining shares and that accordingly the repurchase exercise was integral to a broader scheme to stabilize the price of the shares.

CHAPTER 6

AN ANALYSIS OF MR LI'S DEALING IN THE SHARES OF YUE DA MINING

247. The overwhelming majority of Yue Da Mining shares acquired during the relevant period - from 3 December 2007 to 12 September 2008 - were acquired at the *direct* initiative of Mr Li. These included the acquisitions made through Yue Da Group (HK) and the three "nominee" accounts with HSBC that he operated at his own will. For the reasons set out below, we are satisfied that Mr Li was also fully aware - at the time it was taking place - of Yue Da Mining's repurchase exercise.

248. In summary, at all times Mr Li was perhaps the only person (of whom we have knowledge) who knew the full extent of the various share purchase exercises, more especially their true purpose, and was able, to a very material degree, to exercise control over them.

The Yue Da Group (HK) purchases

249. It was never disputed by Mr Li that at all material times - being a director of the company - he managed the trading account of Yue Da Group (HK) with BOCI Securities. In addition, he said that he was the one who gave instructions to Mr Qian to place trading orders.

250. Yue Da Group (HK) purchased Yue Da Mining shares in two periods of time: first, between 27 December 2007 and 26 February 2008 during which time a total of 3,325,000 shares were acquired at a cost of HK$18,379,522.26;

second, between 24 April and 24 June 2008 during which time a total of 740,000 shares were acquired at a cost of HK$3,606,570.12. Accordingly, the number of Yue Da Mining shares purchased by Yue Da Group (HK) during the relevant period totaled 4,065,000; the total cost being HK$21,986,092.38.

251. In making these purchases, Yue Da Group (HK) enjoyed market dominance.[55] Trading took place on 59 out of 78 trading days, a total of 361 buy orders being placed. As Mr Li accepted, the purpose of the dealing was to acquire Yue Da Mining shares. As to why the decision was made to acquire the shares, Mr Li said that it represented efforts on the part of Yue Da Group (HK) to regain and/or increase its shareholding in Yue Da Mining after the shareholding had been diluted in the placement exercises.[56]

Knowledge of Yue Da Mining's share repurchase exercise

252. The first period of purchasing Yue Da Mining shares (from 27 December 2007 to 26 February 2008) coincided with the period of time in January 2008 (from 16 to 23 January) when Yue Da Mining conducted its repurchase exercise - a matter which we shall examine in the next chapter.

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[55] In his analysis of the trading, Mr Cheng found that between 27 December 2007 and 26 February 2008, Yue Da Group (HK) enjoyed a market dominance of 52.1% and between 24 April and 24 June 2008 a dominance of 20.26% (excluding non-AMS activities).

[56] In his statement to the SFC dated 13 March 2009, Mr Li explained the rationale for purchase by saying (Answer 6): "At that time when the substantial shareholder [Yue Da Group (HK)] decided to increase its holding, major considerations were given to the fact that the substantial shareholder's shareholding had been diluted after the share placement at the beginning of December 2007 and/or the substantial shareholder's reduction of its holding in January 2008, and the underestimation of the company's stock price. As such, an increase in holding would be in the interests of the substantial shareholder and could boost investors' confidence. The decision was made after I had reported it to the leadership of the Group and the decision was also executed by me, that is, by giving instructions to [Mr Qian] to place orders."

253. In his statement of 13 March 2009, Mr Li denied any involvement in and effectively any real knowledge of the share repurchase exercise by Yue Da Mining.[57]

254. We reject that assertion. While Mr Li was not a director of Yue Da Mining, he *was* a director of its controlling shareholder, Yue Da Group (HK), and had signing powers on the bank accounts of Yue Da Mining. Indeed, he was at about that time (between 3 December 2007 and 13 February 2008) removing large sums of money from Yue Da Mining in order to finance his share dealing in the "nominee" accounts of Zhang Hongyan and Su Linian: a matter to which we shall refer shortly. During the course of the hearing nobody suggested that Mr Li was financially foolish. He was after all trusted by the Chairman of the whole Jiangsu Group and, on the basis of all the evidence, had clearly been posted to Hong Kong to protect the interests of the Group. There is simply no basis for thinking therefore that he would have removed large sums of money from Yue Da Mining without having a clear picture of the company's financial position including other calls on its coffers - such as the cost of the repurchase exercise.

255. It is also to be remembered that Mr Li was at that time working together with Mr Qian, a fellow veteran of the Jiangsu Group. The two men worked from the same set of offices. Business travel and the like aside, they

[57] In his statement of 13 March 2009, Mr Li was asked why Yue Da Mining had conducted its repurchase exercise. He answered (answer 7): "At that time, I was just a director and deputy general manager of the substantial shareholder [Yue Da Group (HK)]. I knew almost nothing about the operation of Yue Da Mining, except for taking charge of the public relations and reception affairs, and so I have no idea about this question."

would have seen each other daily. Mr Qian was given the responsibility of conducting the share repurchase exercise, a sum of HK$10 million being initially set aside for that purpose. Both men had signing powers on the bank accounts of Yue Da Mining. The intended disbursal of a significant sum of money on a share repurchase exercise that had been approved by the Chairman of the Jiangsu Group would therefore have been a matter of direct and legitimate interest to Mr Li. There was no reason to prevent Mr Qian informing Mr Li (for example, an issue of confidentiality) and every reason to do so. Indeed, the share repurchase exercise was a *public* exercise, the matter being reported daily to the Stock Exchange.

256. In our judgment, therefore, the probabilities plainly and unequivocally point to the fact that Mr Li would have known of the share repurchase exercise at the time that it took place; indeed, he may well have known of it before it commenced. More than that, taking into account all relevant circumstances, we are satisfied that, if he so wished, he would have had no difficulty obtaining all relevant information as to the share repurchase exercise.

257. In summary, therefore, we are quite satisfied that, when Mr Li authorized the purchase of Yue Da Mining shares by Yue Da Group (HK) and when he dealt in those same shares through the three "nominee" accounts he was aware of the repurchase exercise, whether as a contemporaneous and/or future and/or historical fact.

Dealing in the three "nominee" accounts

258. Mr Li further accepted that he used three so-called "nominee" accounts to trade in Yue Da Mining shares, his trading in those accounts consisting overwhelmingly of acquiring the shares. The "nominee" accounts were in the name of three women: Zhang Hongyan, Su Linian and Zhang Qing, all Mainland residents. Mr Li persuaded these women to set up trading accounts with HSBC in Hong Kong which he then used, he said, for the benefit of associates. Whatever the women may have said later (when the three accounts fell under scrutiny), it is clear that at the time the accounts were being operated by Mr Li they knew nothing of Mr Li's activities in respect of those accounts. As we said earlier, for Mr Li it was a convenient form of disguised trading.[58]

259. We have earlier given an outline of the dealing in Yue Da Mining shares through the three "nominee" accounts. However, to recap -

i. Dealing in the account of Zhang Hongyan took place between 3 December 2007 and 13 February 2008 at a time when Yue Da Group (HK) were purchasing Yue Da Mining shares and Yue Da Mining was conducting its repurchase exercise: both known to Mr Li. A total of 1,388,000 Yue Da Mining shares were purchased by Mr Li through this account. A total of 680,000 shares were sold. This left a credit of 708,000 shares. These 708,000 shares cost HK$5,576,976.00.

ii. Dealing in the account of Su Linian took place between 2 January and 22 April 2008. In that period a total of 994,000 shares were purchased

[58] See paragraphs 93 and 94 in Chapter 2 under the heading: "Dealing in Yue Da Mining shares through the 'nominee' accounts."

by Mr Li. None were sold. These 994,000 shares cost HK$4,992,631.06.

iii. Dealing in the account of Zhang Qing took place between 15 April and 12 September 2008. A total of 1,662,000 shares were purchased by Mr Li. A total of 56,000 were sold. This left a credit of 1,606,000. These 1,606,000 shares cost HK$5,143,277.11.

260. Mr Li's dealing in the three "nominee" accounts resulted in the net acquisition of 3,308,000 Yue Da Mining shares at a total cost of HK$15,712,884.17.

261. In our view, for reasons to which we shall refer shortly, it is important to note that Mr Li's dealings in the three "nominee" accounts related solely to Yue Da Mining shares. No other shares listed on the Hong Kong Exchange were purchased or sold.

Summary of Mr Li's dealings

262. In order to have some idea of the scale of Mr Li's dealing in Yue Da Mining shares during the relevant period, it is to be noted that Mr Li initiated the purchase of 4,065,000 shares by Yue Da Group (HK) at a cost of HK$21,986,092.38. He further initiated the purchase of 3,308,000 shares through the three nominee accounts at a cost of HK$15,712,884.17.

263. At Mr Li's direct initiation, therefore, a total of 7,373,000 shares were purchased at a cost of HK$37,698,976.55. For a share that was not a "blue

chip" and not heavily traded, indeed for most of the time was relatively thinly traded, Mr Li's dealings were significant.

264. What must also be noted is that Mr Li was actively acquiring Yue Da Mining shares immediately before, during and after Yue Da Mining itself was conducting its short-lived repurchase exercise; that repurchase exercise (we are satisfied) being known to Mr Li.

The reasons given for dealing in the three "nominee" accounts

265. We have earlier given an outline of the reasons advanced by Mr Li and another witness, Mr Jiang, for his dealing in Yue Da Mining shares in the "nominee" accounts.[59] In order to recap, the reasons may be summarized as follows:

i. Nanjing Zhongxinyue was at one time a subsidiary of the Jiangsu Group but after restructuring had been set up as an independent corporation. The Deputy General Manager of the company was Mr Jiang.

ii. Nanjing Zhongxinyue was owed money by a Mr Wu Guoyi, a man who seemingly was on friendly terms with Mr Li. Mr Wu offered to clear his indebtedness by making over a portfolio of Yue Da Mining shares held on his behalf by Mr Li in two "nominee" accounts, the one in the name of Zhang Hongyan and the other in the name of Su Linian. Nanjing Zhongxinyue agreed to this arrangement.

iii. Working through the office of Mr Liu Yadong, a senior financial officer with the Jiangsu Group, Mr Jiang was able to contact Mr Li to tell him

[59] See Chapter 2, paragraphs 105 onwards to the end of the chapter.

that Nanjing Zhongxinyue were now the beneficial owners of Mr Wu's Yue Da Mining shares.

iv. At that time, however, the Jiangsu Group was itself indebted to Nanjing Zhongxinyue (the actual indebted company being Jiangsu Yue Da South Holding Company Limited), this debt having been outstanding for some time. In order to clear this debt, it was agreed that repayment would be made with funds being withdrawn principally from Yue Da Mining.

v. However, there would not be a simple transfer of funds to Nanjing Zhongxinyue. Instead, seemingly all of the funds required to clear the debt would be entrusted to Mr Li who would invest them in Hong Kong stocks on behalf of Nanjing Zhongxinyue. The investment of the funds would be through the "nominee" accounts where Mr Wu's Yue Da Mining shares (now made over to Nanjing Zhongxinyue) were held.

vi. As to why it was that only Yue Da Mining shares were acquired by Mr Li for Nanjing Zhongxinyue, Mr Jiang explained that he knew very little of the Hong Kong market and did not know of other Hong Kong shares. In addition, he said that at that time he was confident that Yue Da Mining shares would do well. Mr Jiang said that he was also confident that Mr Li would manage Nanjing Zhongxinyue's share investments well.

vii. In the result, it was the essential thrust of Mr Li's explanation (supported by Mr Jiang) that during the relevant period his dealing in the shares of Yue Da Mining was on behalf of one entity, that is, Nanjing Zhongxinyue. The funds he used to carry out his dealing were funds properly owed to Nanjing Zhongxinyue by the Jiangsu Group.

viii. As to why it was that the funds had come from Yue Da Mining (in order, as it turns out, to purchase Yue Da Mining shares), this was part of the ordinary ebb and flow of funds within the Jiangsu Group. Yue Da Mining had received very substantial sums to assist it and was now releasing some.

Looking more closely to the source of the funding for the "nominee" accounts

266. In his statement of 13 March 2009, Mr Li accepted that finances to pay for the share purchases made through the nominee accounts came (for all intents and purposes) from Yue Da Mining. In this regard, he said (answer 5):

> "It was me who withdrew money from the account of Yue Da Enterprise or Yue Da Mining or Yue Da Group (HK) and then transferred it to them [the nominee accounts]."

267. As to why he was able to do this, Mr Li said (answer 5):

> "The ultimate source of the funds came from the repayment of the amount due to Nanjing Zhongxinyue by Yue Da Enterprise on behalf of the Jiangsu Group. In other words it was Nanjing Zhongxinyue's money. Such a fund arrangement was approved by Liu Yadong, head of the finance department of the Jiangsu Group after mutual negotiations.[60] Otherwise I would definitely not dare to withdraw such a large amount of money privately or bear the responsibility. I can assure you that I have never gained a cent from it."

268. We pause at this juncture to observe the following. The fact that Mr Li was able to tap into the funds held by Yue Da Mining and/or its accounting vehicle, Yue Da Enterprise, and, if required, Yue Da Group (HK), is evidence that at the relevant times he must have had an overall understanding of the funds

[60] According to Mr Li, Mr Liu Yadong had played a part not simply in reaching agreement as to the repayment to Nanjing Zhongxinyue but at the very least had known of the arrangement in terms of which the funds in repayment were diverted to Mr Li's "nominee" accounts.

held by these companies and the dynamics that directed their flow or must have received skilled advice in regard to such matters.

269. We also pause to observe that while the nature of the funds that were moved is obviously relevant, the fundamental issue is not the "legitimacy" of the funds that were used but the intention behind their deployment.[61]

Making payment into the "nominee" accounts

270. In tracing the flow of funds, particularly in respect of funds flowing into Zhang Hongyan's "nominee" account, the SFC discovered a system in terms of which, instead of there being a straight transfer into the account by means for example of a cheque drawn on Yue Da Mining, Yue Da Enterprise or Yue Da Group (HK) in favour of Zhang Hongyan's account, the funds would at some point be translated into cash. For example, in Mr Li's interview statement of 13 March 2009 (question 8) the SFC referred to two separate cash withdrawals totaling HK$1,000,000.00 taken by Mr Qian from Yue Da Mining's account with Standard Chartered Bank on 10 December 2007. On the same day, Mr Qian deposited the HK$1,000,000.00 cash into Mr Li's HSBC account and on the same day Mr Li then transferred that sum into the "nominee" account of Zhang Hongyan.

[61] In Chapter 2, paragraph 63, we said the following: "… if for the sole or primary purpose of supporting a share price (thereby undermining the interplay of genuine market forces) a company builds a war chest by calling in loans that are properly due and/or raises funds by way of loans from associated companies, and then employs those funds for the intended purpose, it seems to us that the company may be culpable of a manipulation of the market."

271. At the very least, of course - absent clear statements contained within the accounts, and we were referred to none - the removal of cash from one account followed by the payment of cash into another broke the chain of evidence as to the flow of funds. Funds were removed in cash from one account without any indication of their onward destination and were then paid into another unconnected account without any indication of their provenance.

272. Why should this puzzling, and indeed worrying, system have been adopted? It was as if Mr Li was seeking to keep the diversion of funds into the nominee accounts hidden. Mr Li attempted to explain this methodology by saying the following:

> "It is mainly because of the financial requirements. If a cheque/or cash is given directly to other persons with whom there are no business dealings, this will contravene the financial requirements and so fund withdrawals must be done by a financially-authorised person. As this matter was co-ordinated and handled by me, they all gave the cash to me."

273. But why the use of cash withdrawals and deposits? Mr Li continued his answer by saying:

> "As to why cash was used instead of cheques, the major consideration was that the time required for cash to be credited in an account is shorter than the time required for cheques."

274. As will be seen, Mr Li qualified his answer by saying that the "major" consideration for the use of cash was speed. He did not, however, condescend to give the lesser consideration or considerations. We are therefore left with the single reason: speed.

275. In the judgment of the Tribunal, the most transparent, straightforward and "regular" way to move funds from Yue Da Mining and/or Yue Da Enterprise into the "nominee" accounts was by way of a simple, easily documented cheque transfer. That must have been known to Mr Li (and to Mr Qian). The sudden translation into cash must have been understood therefore by both men to be (at best) unusual. The need for speed rings hollow, especially when it is remembered that there is a regulated period of grace for payment of all share purchases. In the view of the Tribunal, the only reasonable inference to be drawn is that Mr Li was of the belief at the time that there was a need for a lack of transparency or, to use the description that we have earlier employed, he was seeking to keep his trading "disguised".

276. Some support for this is to be found in Mr Li's interview statement of 13 March 2009. In that statement, Mr Li was asked by the SFC if Mr Dong and Mr Qian were aware of his dealing through the "nominee" accounts. He answered:

> "Regarding the matter about trading Stock 629 [Yue Da Mining] for my friends, I think it is rather sensitive and so I have not told anyone about it. However, I had to inform Mr Qian of the specific purpose every time I made withdrawals. Hence Mr Qian is aware of this. I have not told Mr Dong and other people in the company."

277. But why was the matter so "sensitive", indeed so sensitive that Mr Li did not think it appropriate to inform Mr Dong, the CEO of the company from which, for all intents and purposes, the funds to invest on behalf of Nanjing Zhongxinyue were being drawn? It is not as if Mr Li was acting (within the Jiangsu Group at least) in an unauthorized manner. If he is to be believed, the

whole scheme had been given the blessing of a senior financial officer in the Jiangsu Group, Mr Liu. More than that, the funds being used were legitimately being employed to liquidate a debt due to Nanjing Zhongxinyue and it was the choice of that company that the funds be invested on its behalf in Hong Kong stocks.

278. Yet, if Mr Li is to be believed, he sought to keep secret from the CEO of Yue Da Mining the fact that he was withdrawing literally millions of dollars from the company for the purpose of purchasing Yue Da Mining shares. If all was above board, it is plain that Mr Dong was entitled to know. Yet, according to Mr Li, he was kept in the dark.

279. Why? Mr Li never condescended to explain.

280. Even if there were some concerns that Mainland exchange control regulations may be breached, Mr Dong was the CEO of a Hong Kong listed company that was not itself subject to Mainland exchange control.

281. As to the possible relevance of Mainland exchange controls, Mr Jiang in his statement said something to the effect that he believed the share dealing may contravene Mainland regulations.[62] But Mr Li never touched on that issue. And that still leaves open the question: why was it necessary to disguise

[62] In his statement Mr Jiang explained why he did not simply open a trading account in Hong Kong. He said: "I thought that Mainland people are not allowed to trade Hong Kong stocks. I thought that Mr Li Libin and Mr Liu Yadong would not lie to me."

standard transfers from Yue Da Mining (a Hong Kong listed company) to the "nominee" accounts (held with HSBC in Hong Kong)?

The lack of documentation

282. It is disturbing, in our view, that there was no written evidence of a contemporaneous nature put before us to prove the existence of an agreement in terms of which monies due to be paid to Nanjing Zhongxinyue were diverted for the purposes of acquiring Yue Da Mining shares, Nanjing Zhongxinyue being the beneficial owner of those shares.

283. A formal contract would not be expected. Nor are we blind to the fact that certain businessmen may prefer the security of the word of trusted colleagues to black ink documents spelling out terms and conditions.

284. But the fact remains that no documentation was put before us: no memorandum, no email record, and no note in the papers of Mr Liu Yadong or Mr Li. Nor was any written record put before us of communications - no matter how terse - that took place during the period of Mr Li's acquisition of Yue Da Mining shares ostensibly on behalf of Nanjing Zhongxinyue.

285. Again, it appears that steps were taken to keep the issue of the movement of monies and the acquisition of Yue Da Mining shares essentially disguised.

Why was Mr Li chosen to manage the investments for Nanjing Zhongxinyue?

286. If it is accepted that the funds used to purchase Yue Da Mining shares through the "nominee" accounts were legitimately being deployed to pay a debt to Nanjing Zhongxinyue, and if it is accepted that over HK$10,000,000.00 was deployed in that exercise, it raises the question why Mr Li was not only given control of the exercise but was (almost entirely) left to his own devices as to how he exercised that control.

287. There was no evidence placed before us that Mr Li was an expert in the field or had any particular experience in it. He himself admitted he was no expert. He seems to have been chosen simply because he was already managing a portfolio of Yue Da Mining shares for Mr Wu (a somewhat hazy figure who gave no statement to the SFC).

288. If there was no hidden ulterior motive in the purchase of Yue Da Mining shares, the question must be asked: why wasn't the matter left to professional brokers in Hong Kong? If necessary, an account could have been opened with such brokers in trust for Nanjing Zhongxinyue. The brokers could have been given instructions to acquire Yue Da Mining shares at such rate and at such prices as they thought best in the exercise of their professional discretion. Funds could have been paid direct to them. All monies received by the brokers would have been monies paid to Nanjing Zhongxinyue. A detailed record would have been available at all times not only of the total of monies paid but how exactly (and to what effect) they had been deployed.

289. But that was not done. Instead, the matter was left entirely in the hands of Mr Li who, if he is to be believed, used a lap-top computer (and a "dongle" to get WIFI) in order to place orders. Mr Li, however, accepted that he was no expert in the field of share dealing. Why then take on the responsibility?

290. Importantly, having taken on the responsibility on a good-faith basis in order to help a "friend", Mr Li must have appreciated that he owed a duty of care to Nanjing Zhongxinyue, a duty that would oblige him to give objective advice and, if he believed that the interests of Nanjing Zhongxinyue may be prejudiced if he continued to purchase shares that were inexorably losing their value, to make that known or at least to employ a far greater degree of caution. But there is no evidence of that. We accept, of course, that business people do not necessarily think like lawyers. But acting in good faith on behalf of a friend is not a complex legal concept. It clearly brings with it a responsibility to act in the best interests of that friend. That would have been known to Mr Li, we are sure of it. The fact therefore that he continued throughout on a regular basis to acquire Yue Da Mining shares even though the share price fell into material decline indicates either that Mr Li had no regard for the interests of Nanjing Zhongxinyue or that at all times he had an ulterior motive in purchasing the shares.

291. Equally, the question may be asked: why would Nanjing Zhongxinyue wish to use the services of Mr Li and only his services? And why would it persevere with him even after it must have been obvious that the investment strategy was failing?

292. Mr Jiang said that he traded in Yue Da Mining shares only because he knew very little of the Hong Kong market and did not know of other Hong Kong shares. In addition, he said that he felt confident with Yue Da Mining shares and trusted Mr Li to manage the shares. Mr Jiang, however, was a senior member of Nanjing Zhongxinyue, a man with experience of business. It sounds a little weak for him to say that he had no knowledge of other Hong Kong shares. Such knowledge would have been available to him with the minimum of effort and surely he would have understood that some diversification would stand to protect his company's investment. But no, he invested everything in the single share. More than that, he persisted in that strategy even when the share price fell into a material decline.

293. Mr Jiang said that when necessary he gave instructions to Mr Li concerning the portfolio. For example, he spoke of hearing the news that Mr Hu, the Chairman of the Jiangsu Group, was in very poor health and, in light of that news, instructing Mr Li to sell a portion of the portfolio. That aside, however, no mention of any closer supervision was given. No evidence was put before the Tribunal of any regular discussions as to the health of the portfolio and, as we have mentioned earlier, certainly no evidence of written feedback.

<u>The internal report of the Jiangsu Group</u>

294. It was not only the SFC that conducted an investigation into Mr Li's use of the "nominee" accounts to deal in the shares of Yue Da Mining. The Jiangsu Group itself conducted an internal investigation. Whether this was

done entirely independently of the SFC investigation or was prompted by knowledge of the SFC investigation was not made known to the Tribunal. The internal report, dated 6 February 2009, was given to the SFC.

295. With respect to those who compiled the report, it was not of particular assistance to the Tribunal in determining the issues before it.

296. As to why funds due to Nanjing Zhongxinyue should have been entrusted to Mr Li to invest, the internal report's conclusions follow the explanation of Mr Li and Mr Jiang:

> "Nanjing Zhongxinyue intended to invest in Hong Kong stocks but it didn't have sufficient foreign exchange capital. Therefore Jiang and Li Libin were introduced to each other by Liu Yadong. The three of them agreed upon discussion to make use of the flows of capital between our Group and the company in Hong Kong and Jiangsu Yueda South Holding Company. Limited, i.e. the company in Hong Kong would settle the payments owed to Nanjing Zhongxinyue in HK dollars for Jiangsu Yueda South Holding Company Ltd., as a means of resolving the problem faced by Nanjing Zhongxinyue in finding sources of foreign exchange capital for investing in Hong Kong stocks."

297. As to the fact that only Yue Da Mining shares were acquired, the report said:

> "[As] the natural person shareholders of Nanjing Zhongxinyue including Liu are relatively familiar with the fundamentals of our Group and Yue Da Mining, they [were] confident in the management of the listed company in Hong Kong and [were] particularly optimistic about the prospects of resource stocks upon transformation of the main business of Yue Da Mining, intending to make a long-term strategic investment in Yue Da Mining."

298. The report continued:

> "Upon verification of relevant accounts of the head office of our Group, the company in Hong Kong [Yue Da Mining] and Jiangsu Yueda South Holding Company Limited, it has now been ascertained that: in the period from November 2007 to March 2008, as confirmed by Liu Yadong (offsetting the incomings and outgoings owed to Nanjing Zhongxinyue by Jiangsu Yueda South Holding Company Limited, accordingly to ensure capital safety of our Group),… Li Libin had withdrawn a total of HK$12.84 million from the company in Hong Kong [Yue Da Mining] and deposited the money into three natural persons' accounts specified by Nanjing Zhongxinyue. The entire sum had been recorded as current accounts on the book of the company [Yue Da Mining]. Our Group had then cleared the accounts with Jiangsu Yueda South Holding Company Limited and Jiangsu Yueda South Holding Company Limited had cleared the accounts with Nanjing Zhongxinyue…"

299. On a reading of the internal report, it appears that the full debt owed by Jiangsu Yueda South Holding Company Limited to Nanjing Zhongxinyue had been paid, all the funds (for all practical purposes) coming from Yue Da Mining and all being used by Mr Li to invest in Yue Da Mining shares on behalf of Nanjing Zhongxinyue.

Mr Li's letter to the Tribunal dated 6 July 2013

300. Earlier in this report, we have made mention of the fact that, at the time when Mr Li informed the Tribunal that his physical ailments did not allow him to give testimony to the Tribunal, even by way of video link from near his home, he sent a letter to the Tribunal. That letter was dated 6 July 2013. It has provided the Tribunal with considerable assistance.

301. In the letter (intended effectively to be a plea *in misericordiam*) Mr Li made reference to dealing in Yue Da Mining shares on behalf of his "friends".

He further spoke of the collapse of the share price causing enmity between him and his friends:

> "Pressure from friends. Since great losses have been incurred in the shares brought through me over the years, and are all "being tied up", not only had friendship disappeared among friends, we eventually almost became enemies. They even wanted me to bear and compensate them for part of the losses, adding significantly to my predicament."

302. While we accept that, when great losses have been made, colleagues tend to fall out and while we further accept that who was originally to blame may become obscured, we have some difficulty in reconciling this statement by Mr Li with the evidential material put before us at an earlier stage, indeed put before us largely by Mr Li himself.

303. That is why we have been at some pains to spell out the essentially simple outline of the *asserted* agreement, one that, on its face, could not have led to any misunderstanding:

i. Nanjing Zhongxinyue, a corporation independent of the Jiangsu Group, was owed money by a member of the Jiangsu Group and wished to employ that money to invest in Hong Kong stocks. That the money should be diverted to invest in Hong Kong stocks was therefore the decision of Nanjing Zhongxinyue itself.

ii. The decision to invest solely in Yue Da Mining shares was made by Nanjing Zhongxinyue. According to the Jiangsu Group's internal report, Mr Jiang and other senior members of Nanjing Zhongxinyue were optimistic as to the prospects for Yue Da Mining. There is no

evidence that, against its better judgment, it was prevailed upon to invest only in this single share.

iii. As for Mr Li, he was doing no more than executing the agreement.

304. Why then - if any credit is to be given to Mr Li's plea - should he be blamed in such extreme terms by his "friends" (who can only be the senior management of Nanjing Zhongxinyue) for doing no more than executing *their* wishes? It is another puzzle.

305. In our view, perhaps the most revealing glimpse of the true position is to be found in the following short passage from Mr Li's letter:

> "Since I am not an expert in this, I did not consider if the trades had breached any regulations. I only thought of driving up the share prices. However, not only did the outcome become worse and worse, I even caused such big trouble that I will feel regret for the rest of my life."

306. Two revealing issues arise out of this short passage.

i. Mr Li accepts that he was no "expert" and did not consider whether his share trading on behalf of Nanjing Zhongxinyue breached any regulations (presumably the share trading provisions that are the subject of this report), and, perhaps most revealing of all; and

ii. Mr Li admitted that his intention in trading in Yue Da Mining shares had been one of "*driving up the share prices*".

307. In our judgment, that last statement both defines, and puts into context, the true purpose behind Mr Li's dealing in Yue Da Mining shares not only through the "nominee" accounts but also through Yue Da Group (HK).

Can the Nanjing Zhongxinyue agreement be rejected as an invention?

308. On the evidence, the suspicion must be there that the arrangement to purchase Yue Da Mining shares was concocted after the event, perhaps at a time when it was known that the SFC had commenced investigations. But suspicion is not enough. It must also be remembered that, although Mr Jiang was interviewed by the SFC, no member of senior management of Nanjing Zhongxinyue was given an opportunity to testify or to put papers before the Tribunal. The more profound issue, in our view, goes to the true nature of the agreement. Why, for all intents and purposes was Mr Li personally (and no other person either alone or in conjunction with him) given *carte blanche* to acquire Yue Da Mining shares? Why did Mr Li consider his mandate to be "sensitive", indeed so much so that he intentionally did not inform Mr Dong, the CEO of Yue Da Mining, of the arrangement?

309. As we have said earlier, if Mr Li took on the responsibility of investing on behalf of Nanjing Zhongxinyue, what propelled him to persist in the purchase of the single share even though over many months it was in decline? As we have said elsewhere, the pattern of trading was one of relentless acquisition, dominating the market more often than not in so doing. There appears to have been no attempt to buy and sell in order to make short-term profits or minimise losses.

310. In the view of the Tribunal, whether there was or was not any arrangement in place with Nanjing Zhongxinyue, what is plain is that Mr Li acted as if there was no obligation to that company on his part; to the contrary it

is plain that he acted as if his only obligation was to the welfare of the Jiangsu Group and, at that time more specifically, to attempting to increase, maintain or to prevent the further decline of the value of the shares of Yue Da Mining.

The Tribunal's conclusion as to Mr Li's principal purpose for dealing through the "nominee" accounts

311. In the judgment of the Tribunal, the evidence points plainly to a single conclusion. As Mr Li himself expressed it in his plea to the Tribunal to be no longer bothered with this enquiry, his purpose in acquiring the Yue Da Mining shares through the "nominee" accounts - no matter the nature of his stated obligations to his "friends" - was to drive up the price of Yue Da Mining shares, that is, in a disguised manner to increase, set or maintain their market value and to do so against the forces of genuine supply and demand. That, we are satisfied, was his primary purpose.

312. But why would he wish to do that? In the present case, we think, Mr Li's purpose stands easily explained. He had been given charge of Yue Da Group (HK), Yue Da Mining's controlling shareholder, and given signing powers on the bank accounts of Yue Da Mining (to the exclusion of Mr Dong himself) to ensure the broader interests of the Jiangsu Group. At the time when Yue Da Mining, with the assistance of the Jiangsu Group, was attempting to transform itself into a major player in the Mainland mining sector, was seeking to repay large debts and was meeting investor resistance, it was imperative that the share price be at least maintained. Mr Li acted according to that imperative and did so through the "nominee" accounts.

313. We are satisfied that maintenance of the share price was Mr Li's primary purpose in dealing through the "nominee" accounts. That would not have been the primary purpose of independent Hong Kong brokers. On the clear balance of probabilities, that, we think, was why Mr Li was given, or took upon himself, sole responsibility for dealing through the "nominee" accounts alone.

314. We have found that Mr Li's primary purpose in dealing through the "nominee" accounts was to increase, set or maintain the value of Yue Da Mining shares and to do so against the forces of genuine supply and demand. That finding, however, does not exclude the possibility that the funds used were genuinely due to Nanjing Zhongxinyue. Nor does it exclude the possibility that Mr Li may have believed that in the end result a profit would be made for that company.

315. For the reasons given, the Tribunal is satisfied that Mr Li, in his dealings through the "nominee" accounts, was culpable of two forms of market misconduct, namely, "false trading" and "stock market manipulation".

316. In the view of the Tribunal there is insufficient evidence that Mr Li knowingly entered into any transaction in his dealings in the "nominee" accounts that did not involve a change in beneficial ownership. As we have said, it is at the very least as likely as not that he intended in all his purchases to pass beneficial ownership in the shares acquired to Nanjing Zhongxinyue. Equally, there is insufficient evidence that Mr Li carried out any fictitious or

artificial transaction or created a device in the course of his dealings. Mr Li has not therefore been found culpable of "price rigging".

The assistance or connivance of Mr Qian

317. Mr Qian was the Company Secretary and Financial Controller of Yue Da Mining. Together with Mr Li, he was also an authorised signatory of that company's bank accounts. More than that, he was an authorised signatory of the bank accounts of Yue Da Group (HK), that company being the controlling shareholder of Yue Da Mining. As we have said on several occasions, he was a colleague of Mr Li, both having been posted to Hong Kong from the Jiangsu Group. In his statement to the SFC, Mr Li said that, as his dealings in the "nominee" accounts were "sensitive" he chose not to tell others of it. This included the CEO of Yue Da Mining. However, he *did* tell Mr Qian.

318. More than that, Mr Qian assisted Mr Li in converting funds into cash in order to make payment into the "nominee" accounts. Mr Qian, as Company Secretary and Financial Controller of Yue Da Mining, a publicly listed company, must have appreciated that this was highly irregular; in short, that it demanded an explanation. What explanation could there be? There was never any suggestion of theft of the monies. If there had been, as a veteran of the Jiangsu Group, Mr Qian we have no doubt would have acted to prevent it. In some way, therefore, the funds were being used, as Mr Li believed it to be, for the benefit of the Jiangsu Group. Mr Qian knew full well that Yue Da Mining was going through a major transformation, that it had acquired very significant debt and that the maintenance of its share price was critical to being able to meet that debt without difficulty. He knew full well because he was the Financial

Controller of Yue Da Mining. At the time when he converted funds into cash he also knew of the "nominee" accounts: Mr Li had told him of their existence.

319. For a person to be found culpable of market misconduct by way of assistance or connivance, it must be demonstrated that he not only gave assistance or connived with another person in carrying out acts of market misconduct but did so with the knowledge that such conduct constituted or might constitute market misconduct. At the least, what must be demonstrated therefore is that, in assisting Mr Li, Mr Qian appreciated that what was being done might constitute market misconduct of some kind.

320. For the reasons given, we are satisfied that the single reasonable inference to be drawn from the proven primary facts is that Mr Qian must have known that the diversion of funds into the "nominee" accounts was for a disguised purpose, that disguised purpose being in some way to seek to protect the share price of Yue Da Mining in a manner that, if publicised, would result in an investigation into one form or another of market misconduct.

321. For the reasons given, we are further satisfied that the single reasonable inference to be drawn from the proven primary facts is that Mr Qian must have appreciated that Mr Li was seeking in whatever way was open to him to support the share price of Yue Da Mining, one of the ways being the direct purchase of shares by the controlling shareholder, Yue Da Group (HK). We are therefore satisfied that, when he was given the responsibility of conducting the share purchase on behalf of that company, Mr Qian knew that it was but one strategy in a broader strategy being overseen by Mr Li. In proceeding as he did,

while in possession of such knowledge, at the very least Mr Qian connived with Mr Li.

322. The phrase "might constitute" as contained in section 252(4)(c)(ii) of the Ordinance encompasses a broad span of knowledge but there must be limits. In our view, there must therefore be evidence that demonstrates that Mr Qian knew of the real possibility, although he could not be sure, that Mr Li's actions were constituting some form of market misconduct. In the judgment of the Tribunal that has been proved.

Is Yue Da Mining to be found culpable by reason of Mr Li's actions?

323. As we have pointed out earlier in this report, Mr Li was not a director of Yue Da Mining. Indeed, he held no formal office with that company. On the face of it, he did some public relations work for the company but (to the outside world) that was the apparent extent of it. Formal office, however, while it will always be a highly relevant factor, cannot of itself be solely determinative. If that was the case, it would be simple enough for a company to avoid liability for various forms of market misconduct by ensuring that a cabal within the company, holding no formal office but being confidentially given authority, carries out the market misconduct. Put another way, the corporate veil must be pulled aside and the reality of the situation considered.

324. The reality is that Mr Li was an authorized signatory of the bank accounts of Yue Da Mining (together with Mr Qian) to the exclusion of the CEO, Mr Dong. On the evidence it is apparent that Mr Li and Mr Qian would monitor and operate the flow of funds between Yue Da Mining, Yue Da

Enterprise, Yue Da Group (HK) and the other companies in the Jiangsu Group with minimal, if any, consultation with Mr Dong. This was their area of authority, an authority bestowed upon them by Mr Hu and/or the senior management of the Jiangsu Group. Mr Dong may have signed accounting vouchers but this was invariably after the event in question and the detail given in the vouchers was sparse.

325. In withdrawing funds in repayment of a Group debt to Nanjing Zhongxinyue, Mr Li was therefore acting within the limits of his authority. If Mr Dong had known this, and the coffers of Yue Da Mining had remained viable, there is no reason to think that he would have objected.

326. If, as a favour to Nanjing Zhongxinyue - and with the consent of Mr Liu, a senior financial officer of the Jiangsu Group - funds removed by Mr Li had been invested on behalf of that company, there is no reason to think that this would have fallen outside of the scope of Mr Li's authority, actual or implied.

327. As it is, of course, we have found that, when Mr Li invested the funds on behalf of Nanjing Zhongxinyue, he did so primarily to benefit Yue Da Mining itself by supporting its share price. He was therefore seeking to promote the interests of Yue Da Mining but, as we have found, did so by a means that constituted market misconduct.

328. Did Mr Li have authority to move funds and to invest them legitimately for the benefit of Yue Da Mining? Mr Li was given his position - we have earlier described it as constituting "the power behind the throne" - in

order to protect the interests of the Jiangsu Group. This included the interests of its Hong Kong listed company. If this involved a legitimate means of financial support, we are satisfied that it would be considered to have fallen into the sphere in which he was employed. In the present case, he did the same thing but by illegitimate means.

329. It was argued on behalf of Yue Da Mining that Mr Li was on a frolic of his own. That he so clearly departed from the scope of his employment that Yue Da Mining cannot be held responsible for his actions. While this has not been the easiest matter, we are satisfied that Mr Li at the time saw himself as very much fulfilling his mandate to protect the interests of Yue Da Mining and thereby of the whole Group. Viewed objectively, we are satisfied that a reasonable, fully-informed onlooker would have come to the same conclusion; namely, that Mr Li was acting within the parameters of his authority or, put another way, that, if what he did was legitimate, there would have been no question of his acting beyond his authority or of going on a frolic of his own.

330. In summary, we are satisfied that Mr Li's acts of market misconduct constituted an unlawful mode of doing what he was authorized to do.

331. Accordingly, for the reasons given, the Tribunal is satisfied that, by reason of Mr Li's actions, Yue Da Mining must also be found culpable of "false trading" and "stock market manipulation" but not of "price rigging".

The share purchases by Yue Da Group (HK)

332. As we have said, Mr Li managed the purchase of Yue Da Mining shares - Mr Qian executing the orders - in two periods. The reason, said Mr Li, was perfectly legitimate. It represented efforts on the part of the Yue Da Group (HK) to increase its shareholding after it had been diluted in the top-up placement exercises. The decision to proceed with the purchase exercises was made by Mr Hu, Chairman of the Jiangsu Group.

333. That may be the case. But during the two periods of purchasing, Mr Li, we are satisfied, was aware of a broader exercise of share purchases or repurchases.

334. First, for the reasons given earlier, we are satisfied that he knew of Yue Da Mining's share repurchase exercise which ran from 16 January to 23 January 2008 during which a total of 862,000 shares were acquired at a cost of HK$4,912,042.68.

335. Second, he was himself dealing in Yue Da Mining shares through the three "nominee" accounts:

i. In respect of the account of Zhang Hongyan, he commenced dealing on 3 December 2007, finishing on 13 February 2008 and in that time acquired 708,000 shares at a cost of HK$5,576,976.00.

ii. In respect of the account of Su Linian, he commenced dealing on 2 January 2008, finishing on 22 April 2008 and in that time acquired 994,000 shares at a cost of HK$4,992,631.06.

iii. In respect of the account of Zhang Qing, he commenced dealing on 15 April 2008, finishing on 12 September 2008 and in that time acquired 1.606 million shares at a cost of HK$5,143,277.11.

336. Mr Li's own dealings in Yue Da Mining shares on behalf of Yue Da Group (HK) ran from 27 December 2007 to 26 February 2008 in which period he acquired 3,325,000 shares at a cost of HK$18,379,522.26 and from 24 April to 24 June 2008 in which period he acquired 740,000 shares at a cost of HK$3,606,570.12.

337. The share repurchase exercise conducted by Yue Da Mining itself was, in terms of Hong Kong's prescriptive statutory and regulatory regime, made public. In the result, the investing public was made aware after each day's repurchase of the number of shares acquired, at what price and for what purpose.

338. However, the Yue Da Group (HK) and the "nominee" account acquisitions were not subject to any such requirements. In such circumstances, Mr Li must have appreciated that, taken together, it was virtually certain that they would create a false or misleading appearance of far greater activity in the market by way of genuine supply and demand than was in fact the case. He must further have appreciated that, taken together, they would act to increase, set or maintain the share price and thus create a false or misleading appearance as to price. It follows that, as an experienced businessman, he must have appreciated that these results would induce investors to enter the market by themselves buying Yue Da Mining shares or would, at the least, lull them into believing that shares already purchased could safely be left.

339. Mr Li, however, did not choose to abandon the acquisition of Yue Da Mining shares through the "nominee" accounts. Nor did he choose to delay the commencement of the acquisition exercise on behalf of Yue Da Group (HK). He proceeded with both.

340. In our view, it was not critical for Yue Da Group (HK) to start to acquire the shares when it did. In order to avoid creating the false or misleading appearances that we have just described, the acquisition exercise could have been left to a later date.

341. In our view, with the knowledge in Mr Li's possession of the wider purchasing taking place, the only reasonable inference to be drawn from the proven facts is that it was his primary purpose in acquiring shares for Yue Da Group (HK) in the first period of trading not just to increase the company's shareholding, a matter which could be dealt with later, but rather to help boost the share price. We are satisfied on all the evidence that at that time that must have been his primary motive. If the share price could be held, indeed materially increased, then that could well settle investor confidence.

342. The second period in which Mr Li acquired Yue Da Mining shares for Yue Da Group (HK) *was* later - between late April and late May 2008 - and in respect of that second period we accept that, on the evidence, it is as likely as not that the primary object was to seek to increase the company's shareholding. The Tribunal therefore makes no finding against Mr Li or Yue Da Group (HK) in respect of that second period.

343. However, in respect of the first period, the Tribunal is satisfied that both Mr Li and Yue Da Group (HK) are culpable of “false trading” and “stock market manipulation”.

CHAPTER 7

DID MR DONG KNOW OF ANY DEALING IN YUE DA MINING SHARES CAPABLE OF A STABILISING THEIR PRICE OTHER THAN BY WAY OF THE SHARE REPURCHASE?

Lack of direct evidence

344. The Tribunal received no direct evidence that Mr Dong knew that, in addition to Yue Da Mining's own short-lived share repurchase exercise, other senior figures in the companies that fell under the Jiangsu Group umbrella were purchasing the same shares and doing so insufficient numbers so as to raise concerns of market manipulation.

345. Mr Li never said that he confided in Mr Dong as to his operation of the HSBC "nominee" accounts or that he confided in him as to the purchase of shares by Yue Da Group (HK). Mr Qian, as we have said, gave no evidence of any kind as to this matter, or indeed any other matter. As for Mr Dong himself, he at all times denied any knowledge of the operation of the HSBC "nominee" accounts and said that all he knew of the purchase of shares by Yue Da Group (HK) came to him, not from Mr Li or Mr Qian, but by way of standard returns received well after the event showing the accumulation of shares by major shareholders.

346. None of the documentary evidence - such as accounting vouchers signed by Mr Dong - was of itself sufficiently detailed to constitute direct evidence of any real cogency.

347. In the result, the extent of Mr Dong's knowledge, if any, had to be proved by way of circumstantial evidence, that is, it had to be plainly established as a matter of inference from the proved facts.

348. Having said that, and before moving to look at the circumstantial evidence, we must pause for a moment to briefly describe one evidential "dead end" that was travelled during the course of the enquiry.

The allegation of trading in Zhang Hongyan's HSBC account

349. During the course of the hearing, evidence was put before the Tribunal which, on its face, indicated that, at 2:35 p.m. on 5 December 2007, Mr Dong traded in Yue Da Mining shares using the HSBC "nominee" account of Zhang Hongyan, the account managed by Mr Li. The trading took place via computer at Mr Dong's apartment. If correct, this was very persuasive evidence that Mr Dong knew of a broader scheme to deal in Yue Da Mining shares and participated in that scheme.

350. Mr Dong accepted that he knew Zhang Hongyan, she being a member of the Jiangsu Group human resources department, but denied any knowledge of the fact that she had a trading account with HSBC. He further denied ever using such an account.

351. In order to refute the allegation that he had used the account to deal in Yue Da Mining shares on 5 December 2007, Mr Dong looked to his business commitments that day, his deduction being that, as he was at the time in the

middle of a "road show" put on by Piper Jaffray, he would not have had the time to go to his apartment.

352. As it was, however, the matter was conclusively dealt with by way of technical evidence received from staff at HSBC. Mr Tang Chun Yin, the manager of the software development department at HSBC, the person responsible for technical support in respect of internet banking, testified that the trading data that had been attributed to Zhang Hongyan should in fact have been attributed to a Mr Cai Handong.[63] Put in layman's terms, there had been a glitch in the system. This disposed of any suggestion that Mr Dong had traded in Yue Da Mining shares using the account of Zhang Hongyan.

Looking to the circumstantial evidence

353. Yue Da Mining and its principal shareholder, Yue Da Group (HK), shared offices. This meant that Mr Dong and Mr Li shared offices together with Mr Qian. Such close proximity is of course a relevant factor but, of itself, it cannot be determinative.

354. More important we think, is the nature of the positions held by the three men or, put another way, the reason why they were there. What the evidence plainly shows is that, among the three, Mr Dong was the outsider. He

[63] Mr Cai Handong was a cousin of Mr Dong who also maintained an HSBC trading account. In his interview with the SFC in March 2009, Mr Dong accepted that he operated this account on behalf of his cousin who lived in the Mainland. He said that he saw no conflict as he never advanced information to his cousin concerning the affairs of Yue Da Mining and only ever acted on his cousin's instructions.

As mentioned earlier in this report, at the commencement of the hearing, and on the recommendation of the Presenting Officer, the Financial Secretary's Notice was amended to remove any reference to trading in Yue Da Mining shares by Mr Dong via his cousin's account, there being no evidence of sufficient substance to show that this operation may – alone or with other forms of trading – have constituted market misconduct.

was not a veteran of the Jiangsu Group, a person seconded from the Mainland to protect the interests of the Jiangsu Group; or, as Mr Dong described Mr Li and Mr Qian, an "expatriate". Mr Dong described himself as an expert manager, a person appointed from Hong Kong to protect the interests of shareholders generally not just the interests of the Jiangsu Group. By contrast, Mr Li and Mr Qian both Jiangsu Group veterans, were clearly positioned for a broader purpose; ensuring the broader welfare of the Jiangsu Group.

355. In this regard, it is noteworthy that at the material time, even though Mr Dong was the CEO of Yue Da Mining, he did not have signing powers in respect of the company's bank accounts. These powers were reserved to Mr Li and Mr Qian. As Mr Dong expressed it in his statement of 7 June 2013, this was "so that the Jiangsu Group could be sure of monitoring and exercising control over the company's [Yue Da Mining's] cash balances".

356. Mr Qian was the Company Secretary and Financial Controller of Yue Da Mining but in addition was an authorized signatory of the bank accounts of Yue Da Group (HK) and was authorized to operate the securities trading account of Yue Da Group (HK). Mr Li was a director of Yue Da Group (HK), essentially its responsible officer. Mr Dong, however, aside from having no signing powers on his own company's bank accounts, held no position of any kind in Yue Da Group (HK). The architecture was plain. Mr Dong, as he said, was there to provide expert management of the Hong Kong listed company, Yue Da Mining. Mr Li and Mr Qian, on the other hand, were brought down to Hong Kong to ensure the broader interests of the Jiangsu Group which of course included the interests of Yue Da Mining itself.

357. It was Mr Dong's assertion, which we have no reason to doubt, that Mr Li was held in high trust by the Chairman of the Jiangsu Group.

358. In his statement of 7 June 2013, Mr Dong said that, because of the broader responsibilities of Mr Qian and Mr Li, they would sometimes sign Yue Da Mining cheques without his prior approval of knowledge.

359. At first blush, it seems strange that Mr Dong would permit the outflow of funds from Yue Da Minging without query or apparent concern. However, as he explained, he was aware of the fact that Yue Da Mining had received substantial sums from the Jiangsu Group through Yue Da Group (HK) and that any flow of funds back from Yue Da Mining was therefore repayment and how that repayment, once made, was then deployed was not a matter of concern for him.[64] His concern, he said, was to ensure that the account balances remained viable and he would ask Mr Qian to confirm that. In addition, the half yearly management reports assured him of the position.

360. Mr Dong dismissed any suggestion that the flow of funds from Yue Da Mining via Yue Da Enterprise back to the Jiangsu Group was - to his knowledge - to provide money for the clandestine purchase of Yue Da Mining shares. To

[64] The expert report of John Lees dated 8 February 2013 supports his evidence. Mr Lees found that Yue Da Mining's current account balance with Yue Da Enterprise, and therefore the Yue Da Group (HK), remained close to zero or in credit until November 2007 when it shifted to material credit value until about March 2008. We note that the increase credit value corresponded with the receipt of funds from Jiangsu Group via Yue Da Group (HK) to assist with the mining acquisitions. As the amounts owed were repaid so the credit value decrease. In this regard, in paragraph 4.3.4 of his report, Mr Lees commented: "On the basis that the current account balance was close to nil or in credit throughout the Review Period, it would appear that any transactions made by Yue Da Mining during this period relate to the repayment of amounts owed by Yue Da Mining to … the Jiangsu group."

his knowledge, he said, it was to repay funds earlier advanced to Yue Da Mining by the Jiangsu Group. Again, however, whether - the payment having been made for that purpose - it was thereafter used for some other purpose was unknown to him.

361. Put succinctly, it was Mr Dong's evidence that the frequent flow of funds was, to his understanding, related to funds advanced to Yue Da Mining and to their repayment, the control of such fund flows being the responsibility of Mr Li working with Mr Qian, they being responsible for looking to the broader interests of the Jiangsu Group. How they dealt with repayments made by Yue Da Mining was a matter for them.[65]

The signing of vouchers

362. Mr Dong said that, largely as a matter of respect, he was given the authority to sign Yue Da Mining accounting vouchers. However, as he travelled frequently, more often than not cheques would be signed by Mr Qian or Mr Li and the funds transferred without any reference to him. He would be left to sign the relevant vouchers - which themselves lack detail - after the event. In the course of his evidence, Mr Dong said that he only recalled one occasion when he was asked to sign a voucher on the date of the transaction and that was when he was personally approached by Mr Li. The evidence indicated that

[65] In the course of his evidence, Mr Cheng, the SFC expert, suggested that the inter-related financial affairs of Yue Da Mining and Yue Da Group (HK) were managed – contrary to best practice – as if they were one entity. There was however no cogent evidence that the system adopted by the two companies, using Yue Da Enterprise, was, conceptually at least, professionally unacceptable. Mr Lees said nothing to that effect. Whether there were isolated instances of a failure to follow professional best practice is of course another matter. In any event, while a failure to follow best practice may be a window to matters that are suspect, the issue for our consideration was whether, by looking to the system, Mr Dong's evidence that he did not know what happened to the funds coming from his company after they were paid, would be exposed as false. We have been unable to establish any such fact by way of inference.

very few vouchers were presented to Mr Dong for signature, indeed just 21 were put into evidence.

363. As Mr Brewer, Mr Dong's counsel, pointed out, nothing whatsoever appears on the vouchers to suggest that the funds in question were destined to be used to purchase Yue Da Mining shares either by Yue Da Group (HK) or by Mr Li in his management of the HSBC "nominee" accounts.

364. In our judgment, the "vouchers evidence" did not therefore advance matters.

Conclusion

365. Earlier in this report, we spoke of Mr Li appearing to be the power behind the throne. Nothing has been put before us from which we can draw the inference that Mr Dong himself was in a similar privileged position. To the contrary, on the evidence, it would appear that Mr Dong was, as we have earlier described him, "the outsider".

366. The weight of the evidence suggests that Mr Dong appreciated that the transformation of Yue Da Mining was not possible without the financial assistance of the Jiangsu Group. As to the day-to-day flow of funds arising out of that assistance the weight of the evidence further suggest that Mr Dong appreciated that this was the responsibility of Mr Li, working with Mr Qian. His authority (remembering that he did not even having signing powers on the Yue Da Mining bank accounts) did not reach that far.

367. In respect of the flow of funds, it was the central thrust of Mr Dong's evidence, as we have comprehended it, that Mr Li and Mr Qian worked together often without consulting him. If that was the case - and we have no basis for disputing it, then the question must be asked: why would Mr Li and/or Mr Qian wish to consult with him as to the use to which the funds removed from Yue Da Mining were to be put? Mr Dong gave evidence that they did not consult him or did he think it appropriate to enquire. Mr Li said nothing of bringing Mr Dong into the picture in respect of his dealing in shares through Yue Da Group (HK) and through his HSBC "nominee" accounts. In the face of such evidence, and in light of our finding that Mr Dong was "the outsider", we have no basis for finding as a plainly established inference that Mr Dong must known that his share repurchase exercise was part of a broader scheme to acquire Yue Da Mining shares in order to stabilize the price during a critical period in the company's history.

CHAPTER 8

SUMMARY OF THE TRIBUNAL'S FINDINGS

368. In the Notice of the Financial Secretary dated 16 December 2011, this Tribunal was required to determine the following two matters going to culpability:

i. Whether any market misconduct has taken place.

ii. The identity of every person who has engaged in market misconduct.

369. For the reasons given in the body of this report, the Tribunal has determined that market misconduct within the meaning of section 274 ("false trading") and section 278 ("stock market manipulation") of Part XIII of the Ordinance has taken place arising out of dealings in the shares of Yue Da Mining (Stock Code 629).

370. The Tribunal has determined that the identity of the persons (including corporate persons) who engaged in such market misconduct is as follows: Mr Li, Mr Qian, Yue Da Mining and Yue Da Group (HK).

371. One further individual was specified in the Notice of the Financial Secretary, namely, Mr Dong. For the reasons given, the Tribunal does not find Mr Dong to be culpable of market misconduct.

372. The Tribunal has not identified any person not specified in the Notice of the Financial Secretary as being culpable of market misconduct.

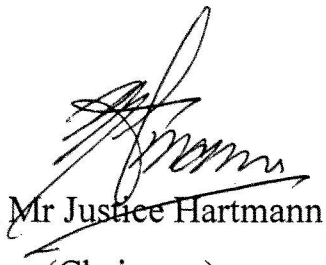
373. As to the nature and extent of the market misconduct, the Tribunal has come to the following findings:

i. Mr Li and Yue Da Mining, with the assistance or connivance of Mr Qian, dealt in the account of Zhang Hongyan with HSBC between 3 December 2007 and 13 February 2008, acquiring a net total of 708,000 Yue Da Mining shares at a cost of HK$5,576,976.00. This dealing constituted market misconduct by way of false trading and stock market manipulation.

ii. Mr Li and Yue Da Mining, with the assistance or connivance of Mr Qian, dealt in the account of Su Linian with HSBC between 2 January and 22 April 2008, acquiring a total of 994,000 Yue Da Mining shares at a cost of HK$4,992,631.06. This dealing constituted market misconduct by way of false trading and stock market manipulation.

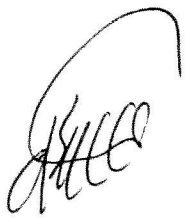
iii. Mr Li and Yue Da Mining, with the assistance or connivance of Mr Qian, dealt in the account of Zhang Qing with HSBC between 15 April and 12 September 2008, acquiring a net total of 1,606,000 Yue Da Mining shares at a cost of HK$5,143,277.11. This dealing constituted market misconduct by way of false trading and stock market manipulation.

iv. Mr Li and Yue Da Group (HK), with the assistance or connivance of Mr Qian, purchased Yue Da Mining shares for the account of Yue Da Group (HK) between 27 December 2007 and 26 February 2008, acquiring a total of 3,325,000 Yue Da Mining shares at a cost of HK$18,379,522.26. This dealing constituted market misconduct by way of false trading and stock market manipulation.



The Hon Mr Justice Hartmann NPJ

(Chairman)



Dr Norman W Y Ngai

(Member)

Dr Cynthia K L Lam

(Member)

Dated 8 May 2014