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Application No. 13 of 2009

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IN THE SECURITIES AND FUTURES APPEALS TRIBUNAL

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IN THE MATTER of a Decision
made by the Securities and Futures
Commission pursuant to s 194 of
the Securities and Futures
Ordinance, Cap 571,

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IN THE MATTER of s 217 of the
Securities and Futures Ordinance

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BETWEEN

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ZHANG XIAO MING

Applicant

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and

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SECURITIES AND FUTURES COMMISSION

Respondent

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Before: Chairman, Hon Saunders J,
Members, Professor Ho Yan Ki, Richard, and Mr Wu King Cheong,
Henry, BBS, JP

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Date of Hearing: 23 July 2010

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Date of Decision: 18 February 2011

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DECISION

Introduction:

1. On 6 February 2008, the SFC issued to Mr Zhang a Notice of Proposed Disciplinary Action (NPDA) informing him that it was considering taking disciplinary action against him under the SFO. That proposed disciplinary action arose out of the activities of ICEA Capital Ltd and ICEA Securities Ltd in the listing of Lang Chao International Ltd (Lang Chao) and Dawnrays Pharmaceutical (Holdings) Ltd (Dawnrays) on the Stock Exchange of Hong Kong.

2. As a result of the preliminary findings made against Mr. Zhang in the NPDA the SFC proposed to prohibit Mr. Zhang from being licensed, for life.

3. Mr Zhang made submissions to the SFC in response to the NPDA, and on 19 November 2009, having considered those submissions, the SFC, by a Notice of Final Decision, (NFD) notified Mr Zhang, first that it did not propose to proceed with the complaints in relation to Dawnrays. However in relation to the Lang Chao matter, the NFD informed Mr. Zhang that the SFC maintained their preliminary findings. The precise findings against Mr Zhang were set out in paragraphs 13 & 14 of the NFD in the following terms:

“13 Accordingly, we find that you had:

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(a) failed to discharge his general duties as a director of ICEA Capital Ltd, (ICEAC), and the top decision maker of ICEAC, and ICEA Securities Ltd, (ICEAS); and

(b) acted inconsistently with General Principles 1 (honesty and fairness), 7 (compliance) & 9 (responsibility of senior management) of the Code of Conduct and paragraphs 3.1 (integrity) of the CFA Code of Conduct.

14. In addition, to the above, we consider you were in breach of sections 274(1)(b), 274(3), 295(1)(b) and 295(3) of the SFO because you instructed your subordinate, William Chen, to trade shares of Lang Chao for the purpose of providing market support to the share price of Lang Chao in the aftermarket. As such, you had procured (i.e. procured by endeavour) and caused your subordinate, William Chen to trade the shares of Lang Chao with the intention that the trades would have, would (be) likely to have, the effect of creating a false or misleading appearance with respect to the market for, or the price of dealings in shares of Lang Chao, in breach of sections 274(1)(b), 274(3), 295(1)(b) and 295(3) of the SFO. You also breached sections 274(3) and 295(3) of the SFO by procuring and causing William Chen to trade Lang Chao shares with the intention that these trades would have, or would (be) likely to have, the effect of creating an artificial price or maintaining a price at a level that is artificial.”

4. As a result of that finding, the SFC concluded that Mr Zhang was not a fit and proper person to be or to remain licensed under s 194 of the SFO. He was accordingly prohibited, a period of 12 months, pursuant to s 194(1)(iv) (A), (B), (C), and (D) of the SFO from:

- i applying to be licensed or registered;
- ii applying to be approved under section 126(1) SFO as a responsible officer of a licensed corporations;

iii applying to be given consent to act or to continue to act as an executive officer of a registered institution under s 71C of the Banking Ordinance; and

iv seeking through a registered institution to have his name entered into the register maintained by the Monetary Authority under s 20 of the Banking Ordinance as that of a person engaged by the registered institution in respect of a regulated activity.

5. Mr Zhang now applies to this Tribunal to review that decision.

The factual background:

6. Mr Zhang was first registered as a securities dealing director of ICEA Capital on 18 February 2003. From 1 April 2003 until 18 November 2003, he was a Responsible Officer of ICEA Capital and held a deemed licensed to carry on Type 1 (dealing in securities), Type 4 (advising on securities) and Type 6 (advising on corporate finance) regulated activities. From 2002 until early 2005, he was a director of ICEA Capital. In August 2002, he joined ICEA Holdings as a member of the senior management and in September 2003, he became its Chief Executive Officer. He was responsible for the overall management and control of ICEA Holdings and its subsidiaries including ICEA Capital and ICEA Securities. He left the group in late 2004 and is now the General Manager of the International Business Department of the Bank of Communications in the PRC.

7. Lang Chao, (currently known as Inspur International Ltd, stock code 8141), is a company engaged principally in the distribution, sourcing and reselling of computer components and related products in the PRC, Hong Kong, Taiwan and Singapore. Lang Chao was listed on the Growth Enterprises Market Board (GEM Board) of the Stock Exchange of Hong Kong Ltd (SEHK) on 29 April 2004, by placing 100 million new shares at \$0.36 per share. ICEAC was the joint sponsor, the Bookrunner and Lead Manager in the listing of Lang Chao.

8. On the first two days of listing, a substantial portion of trading in Lang Chao shares came from a company called Positive Strategy Ltd (PSL). The investigation by the SFC revealed that PSL was in fact a special vehicle set up by ICEAC to conduct proprietary trading.

9. The investigation by the SFC showed that PSL's purchases accounted for 86% of the market turnover of 29 April 2004 and 39.5% of the market turnover on 30 April 2004. Many of these purchases were conducted by way of manual cross trades with clients of ICEAS. PSL did not sell any Lang Chao shares on the first day of listing. In particular the following activities were noted by the SFC:

(i) 10:00:06 a.m. on 29 April 2004, PSL purchased 11,488,000 shares from 88 of ICEAS's clients at \$0.365, one spread above the issue price of \$0.360;

(ii) among the 88 ICEA clients who sold their shares to PSL, 87 were retail clients of the Wanchai branch of ICEAS. These 87 retail clients sold a total of 8,712,000 shares representing

95.7% of the total number of shares allotted to 93 retail clients of the Wanchai branch;

(iii) since the purchase was by way of mutual cross trading and took place immediately after the commencement of trading on the first day of listing, the purchase must have been prearranged before the listing; and

(iv) PSL also conducted manual cross trades with other ICEAS clients in the aftermarket. PSL adopted a “buy high, sell low” pattern in some of the manual cross trades.

10. The SFC were of the view that at least some of the purchase transactions by PSL were made with the intention of providing, or attempting to provide market support for the share price of Lang Chao. It was of the view that the available evidence suggested that before the listing of Lang Chao, ICEAC and ICEAS had made a deliberate decision to provide market support the share price of Lang Chao and the aftermarket through proprietary trading by PSL.

11. Investigation undertaken by the SFC led the SFC to conclude that Mr Zhang was the person who made the final decision to provide market support subsequent to the Lang Chao listing.

12. The SFC relied upon three witnesses in particular, Gary Sik, the former head of investment banking, and a responsible officer and director of with ICEAC, William Chen, the former head of China sales and bonds, ICAES, and Dixon Cheng, former senior vice president of ICEAC.

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13. Gary Sik's evidence to the SFC was that Mr. Zhang was the CEO of ICEAC, and was responsible for managing the operations of ICEAC and ICEAS. In particular listing project at issue Gary Sik said that Mr. Zhang was responsible for directing and coordinating the work of ICEAC and ICEAS. Gary Sik said that he spoke to Mr. Zhang a few days before 26 April 2004, mentioning that market sentiment was not good, and that the placement was barely oversubscribed. Mr. Zhang suggested that ICEA might need to give support to the shares in the aftermarket.

14. William Chen told the SFC that after the issue price of \$0.36 was set, his clients were unhappy and considered the shares overpriced. He said that he was instructed by Mr. Zhang to provide market support and price support the shares in Lang Chao by using the PSL account.

15. Dickson Cheng said that at a meeting of 13 April 2004, Mr. Zhang told a meeting that demand for the shares was insufficient and told the participants to buy the shares from the secondary market, which Dickson Cheng understood meant to provide market support for the shares. In a casual meeting a few days before the listing at which Mr. Zhang attended, Dixon Cheng heard Mr. Zhang formally authorised William Chen to buy Lang Chao shares through a propriety account and that he approved a specific amount for the purchase.

16. The head of legal and compliance at ICEA, Eugene Lee gave evidence to the SFC that no one had ever asked him or his colleagues in the compliance department whether it was proper to use the proprietary account to purchase the shares in Lang Chao.

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17. An approval memorandum, dated 29 April 2004, entitled “ICEA Finance Holdings Ltd Securities Trading Management Committee - Approval of new ICEA Proprietary Trading Activities (for Lang Chao International Ltd)” signed by Mr. Zhang and others, authorised William Chen to conduct proprietary trading for ICEA and approved \$6 million to trade the shares of Lang Chao.

18. On the basis of that evidence the SFC determined that, on 29 April 2004, before the listing of Lang Chao:

- (i) Mr. Zhang was fully aware that the subscription of Lang Chao shares was not popular;
- (ii) that he made a decision to purchase the shares of Lang Chao, and the purpose of the purchase was to support the share price in the aftermarket;
- (iii) that he approved a budget of \$6 million for the purchase; and
- (iv) that he authorised William Chen to buy Lang Chao shares through ICEA’s proprietary account.

19. In considering whether or not Mr. Zhang was a person involved in the management of the business of ICEAC and ICEAS, the SFC had regard to the following factors:

- (i) Mr. Zhang was the Chief Executive Officer of ICEA (which includes ICEAC and ICEAS);

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- (ii) he was a director of ICEAC; he was involved in the central direction of corporate affairs at ICEAC and ICEAS; and
- (iii) he was the final decision maker of ICEAC and ICEAS and other staff had to follow a comply with his instructions and decisions.

20. Upon the whole of the evidence the SFC made the determination is set out in paragraph 2 above.

21. The essence of the finding by the SFC was that Mr. Zhang had instructed ICEA Capital and ICEA Securities to buy shares of Lang Chao for the purpose of providing proper market support for the share price of Lang Chao in the aftermarket, and further that he had taken part or was concerned in, directly or indirectly, the use of a proprietary account in the name of PSL to purchase shares Lang Chao which had, or was likely to have, the effect of reducing the selling pressure on Lang Chao shares in the aftermarket, thus affecting and giving the market a false or misleading impression of the natural supply of and demand for, and the price of, Lang Chao shares.

The decision under s 274 SFO:

22. As is seen from paragraph 2, the SFC considered that these activities were in breach of particular provisions of ss 274, and 295, SFO.

23. Mr. Beresford properly pointed out that s 274 creates an offence of market misconduct which must be determined by the Market

Misconduct Tribunal. Where market misconduct is determined by the Market Misconduct Tribunal, by s 284 SFO, such conduct is deemed to constitute a contravention of the provisions of the SFO. However in the present case there has been no finding by the Market Misconduct Tribunal and consequently deemed conduct under s 284 cannot exist. Technically therefore the finding of a breach of s 274 by the SFC was wrong, and that finding must be, and is, set aside.

24. But at the end of the day, it makes no difference, because the SFC were perfectly entitled to find that Mr. Zhang's conduct amounted to the offence of false trading under s 295 SFO. It is not necessary for there to be a criminal finding by a court that offence has taken place, for the SFC to conclude that conduct equivalent to that offence has taken place, and to rely upon that conduct a disciplinary purposes. The substance of the decision accordingly remains.

The evidence of the SFC witnesses:

25. Mr. Zhang elected not to require any witnesses to be called before us, and did not challenge in evidence any of the evidence from the SFC witnesses, as contained in their statements to the SFC. Instead he preferred to rely upon written submissions placed before us, and he did not attend the hearing.

26. Mr. Zhang was perfectly entitled to conduct the application for review in that way, but when application is on paper and witnesses are not called, it is incumbent upon the applicant to demonstrate that some error has occurred in the proceedings before the SFC or its decision. No such

error is demonstrated here. Mr. Beresford was perfectly entitled to refer us to the following passages from the Tribunal's decision in Cheung Kwok Shing Godwin, SFAT 1/2009:

“The role of the Tribunal on an appeal:

First, Mr Westbrook SC, for the SFC, properly reminded us of the role of the Tribunal, and the principles under which it acts in reviewing decisions of the SFC. He drew our attention to the decision of the Tribunal, in *Wong Ting Choi, Joe 5/2007*, 8 May 2008, (Stone J presiding), and in particular paragraphs 52-71 thereof. The Tribunal is not a regulator of the market; it plainly does not have the competence to act as such. At paragraph 53, Tribunal said:

“The Tribunal will interfere with the discretion of the regulator in its disciplinary function only when it considers that, for whatever reason, something clearly has gone badly wrong and/or where the applicant can demonstrate clear injustice.”

Mr Westbrook further reminded us that this was a case in which Mr Chu elected not to give evidence before us. Under s 219 SFO, the Tribunal has a wide power to receive and consider any material by way of evidence. That must include oral evidence from an applicant for review. Mr Westbrook said this in his opening submissions:

“23 Where an applicant seeks review for insufficiency of evidence, he faces a high hurdle if he gives or calls no evidence on the review. SFO section 219 provides for this Tribunal to receive evidence, but if the applicant does not avail himself of this, the Tribunal is left in the same position as an appellate court hearing an appeal from a court of first instance. The SFC having made its findings after seeing and hearing the witnesses and reviewing their statements, the Tribunal would not be justified in interfering unless it is satisfied that the SFC was plainly wrong in that there was no evidence or basis to support such a finding or the SFC had overlooked any material evidence in favour of the applicant or that it had misdirected itself as to the effect of the evidence.”

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In the present case the applicant confined himself to calling expert evidence, for two purposes. First, his expert sought to demonstrate that expert evidence from the SFC was unreliable. Second, the expert sought to demonstrate that the SFC had misdirected itself as to the effect of the primary evidence.

Mr Chu, was perfectly entitled to conduct the case in this way, and not give evidence himself. As will be seen, we have carefully considered the expert evidence called. But in so far as the application for review sought to challenge a finding of fact, Mr Westbrook was entitled to make the submission he did as to the absence of evidence from Mr Chu or any other witness challenging the fundamental facts found upon which the decision was made. An expert witness, with no personal knowledge of fundamental facts is not in a position to make a challenge to those facts. In reaching our conclusions on the review we have taken this matter into account.

The submission was made that the SFC was required to take into account Mr Chu’s “clear and consistent” denials that he had engaged in any market manipulation. We were further invited to have regard to Mr Chu’s explanations of his intention to execute the orders when performing the trades.

There is nothing in the evidence, and nothing was put to us, to suggest that the denials, or the explanations contained in the course of his records of interview, were not taken into account by the SFC in their consideration.

Because Mr Chu did not give evidence, the assertions by way of denial and explanation made by him in those interviews have not in any way been tested in cross-examination. The fact that those denials were consistent does not, when the denials are not tested in cross-examination, greatly assist an appellant. The fact that explanations might have been given, again does not, when the explanations have not been tested in cross-examination before us, assist an appellant.”

27. The sentiments set out there as to the consequences of the absence of evidence from the applicant, and that the evidence of the SFC witnesses were not tested in cross-examination, apply equally here.

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Discussion:

28. In his submissions Mr. Zhang raises a number of points which we will deal with, seriatim.

29. Mr. Zhang says that he had a passive role at ICEA, that he had no choice in accepting the assignment, and that he had no relevant experience or professional training. We accept Mr. Beresford's submission that the statement is merely a confession of failure on the part of Mr. Zhang to meet the requirements of s 129 SFO, and the standards of a fit and proper person. It is not a matter which in any way challenges the findings by the SFC.

30. Next, Mr. Zhang says that he acted within the scope of the company's authorisation, and consequently should not be held personally responsible. Again we accept Mr. Beresford's submission that in making this assertion Mr. Zhang confuses his responsibility to ICEA and his responsibility as a licensed person. Merely acting with the authorisation or within the scope of the powers arising from his position can never be an answer to improper conduct.

31. Mr. Zhang asserts that the SFC's views have been coloured unfairly by ICEA's previous disciplinary history. There is nothing in the decision under challenge to indicate that the SFC had any regard at all to any previous disciplinary history relating to the company.

32. In response to numerous passages of the decision under challenge, Mr. Zhang says that he has no recollection of the events. That

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he has no recollection has been made up for amply by the unchallenged evidence of the witnesses interviewed by the SFC. That Mr. Zhang cannot remember a matter does not justify a requirement that further witnesses other than those relied upon by the SFC should be produced. The SFC were perfectly entitled, particularly in the absence of any challenge by Mr. Zhang, to rely upon the witnesses they interviewed.

33. Mr. Zhang contends that in the absence of minutes evidencing the meeting on 13 April 2004, (see paragraph 15 above), there is insufficient evidence of the meeting. In fact the meeting was evidenced in an exhibit that was put to Mr. Zhang in the course of his interview on 11 March 2006. He did not then deny the meeting. In the absence of any other evidence we are satisfied that the meeting took place, and that what was recorded in the minutes reflects the events of the meeting.

34. Mr. Zhang argues that the SFC was wrong to rely upon Dickson Cheng’s “understanding” of what Mr. Zhang intended in the conversation referred to in paragraph 15 above. But there is nothing inherently unfair about such reliance, especially in the present case where Mr. Zhang does not seek to put to the tribunal any alternative meaning.

35. Mr. Zhang says that Gary Sik, Dickson Cheng, and William Chen have colluded with each other and had reasons to lie because they knew that the legal liability for acting on instructions was different to that from acting on their own free will. The submission reflects Mr. Zhang’s misunderstanding that regulatory liability cannot be evaded merely because a person is acting on the instructions of another. In any event, William Chen and Gary Sik have been subjected to disciplinary action by

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the SFC for their role in acting upon Mr. Zhang’s instructions in the Lang Chao trading.

36. In his written submissions Mr. Zhang attempt to argue that his participation in the Lang Chao IPO was limited and even goes so far as to say that he did not have any participation in the IPO at all. First, in the absence of evidence from Mr. Zhang before us the submission is simply not open to him. Second, the submission is entirely inconsistent with the representations he has made as to his involvement in the IPO. Further, it is equally inconsistent with his position in the company and the documentary evidence. The mere fact that he may not have been aware of the specific transactions undertaken does not relieve him of responsibility in the face of the undeniable fact, and the clear finding that he had given the instructions for the share price support operation to proceed.

37. Mr. Zhang argues that the conclusion that “ICEA decided to repurchase shares from the client at a price higher than the initial public offering price” is not justified on the evidence. But it is perfectly well supported by the trading activities set out in the NPDA, Gary Sik’s evidence, and William Chen’s evidence. The trading activities are set out at paragraph 9 above. There was more than ample evidence to support the conclusion. But there was clear evidence to support the conclusion by the SFC that the proprietary trading through PSL by ICEA in the aftermarket was to support the price of the Lang Chao shares.

38. Throughout his submissions Mr. Zhang confuses his responsibility to the company, with his responsibility as a licensee under the legislation. His responsibility as a licensee and the requirement that he

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must act with propriety surpasses any obligation that he might have to the company. If he was instructed by the company to undertake activity which, as in the present case, would constitute a breach of a provision of the SFO, in this case the creation of a false market contrary to s 294, it is the responsibility of the licensed person to refuse to undertake the activity. The licensed person must refuse to do so even at the cost of his job.

39. Mr. Zhang asserts that there were no “victims” of trading complained of, nor were there any complaints from investment clients. The submission simply misses the point. The primary victims of false trading are those who may have purchased shares believing that the trading activity demonstrated was genuine trading activity and that there was a genuine interest in the shares. In fact, the trading activity was false and was devised by ICAC and Mr. Zhang to give a false impression of a market in the shares. The secondary victims of the conduct complained are, first, the integrity of the market, second, the public’s confidence in the market, and the cost of equity in the market. Mr. Beresford quite rightly makes the point that traders who incurred an opportunity cost as a result of false trading are unlikely to be aware that they have made their expenditure upon the basis of false trading and consequently complain, simply because of the deceptive nature of the conduct.

40. The essence of the final submission made by Mr. Zhang is that he has been discriminated against as a foreigner, and that his treatment was inconsistent when compared with the treatment of ICEA’s Chief Executive in another disciplinary matter, Euro-Asia. While making the assertion he does not substantiate it in any way by demonstrating any inconsistent treatment between the two transactions. Having elected to put nothing

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before is in relation to the Euro-Asia matter we are quite unable to say that there was any discrimination, much less discrimination based upon the fact that Mr. Zhang came from the mainland.

41. Mr. Zhang asserts that he has learnt a lesson by this matter. We accept Mr. Beresford's submission that that does not appear to be the case because Mr. Zhang's submissions to us demonstrate quite plainly that he does not accept responsibility for what has occurred nor does he demonstrate any proper understanding of the need to protect the integrity of the market and to maintain the rules against false trading.

42. There is no basis at all upon which we can interfere with the decision made by the SFC, whether as to the findings it reached or as to the penalty imposed. The application for review is accordingly dismissed.

Costs:

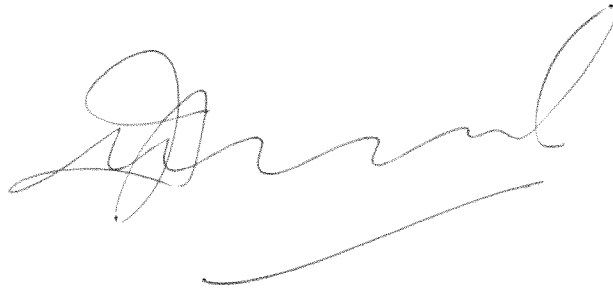
43. There will be an order nisi to be made absolute in 28 days, but Mr. Zhang must pay the costs of the SFC on the application for review, to be taxed in the party and party basis. If Mr. Zhang wishes to challenge the order for costs he must do so within 28 days of the date on which this decision is handed down.

Finally:

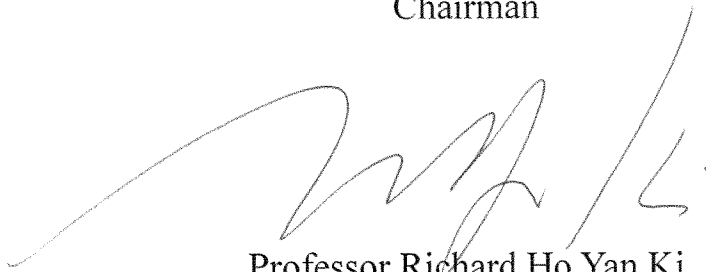
44. It has taken an inordinately long time for this decision to be made. Responsibility for the delay lies entirely with Chairman who expresses his apologies to the parties for the delay.

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John Saunders
Judge of the Court of First Instance
High Court
Chairman



Professor Richard Ho Yan Ki
Member



Mr Henry Wu King Cheong BBS JP
Member

The Applicant in person(absent)

Mr. Roger Beresford, instructed by the Securities and Futures Commission
for the Respondent