Application Nos. 3, 4, & 5 of 2006

IN THE SECURITIES AND FUTURES APPEALS TRIBUNAL

IN THE MATTER OF a Decision made by the Securities and Futures Commission under section 56 of the Securities Ordinance, Cap. 333 and section 36 of the Commodities Trading Ordinance, Cap.250

AND IN THE MATTER OF section 217 of the Securities and Futures Ordinance, Cap. 571

BETWEEN

CHOY YE KING, ANDY	1st Applicant
CHENG KAI MING, CHARLES	2nd Applicant
LI KWOK CHEUNG, GEORGE	3rd Applicant
and	
SECURITIES AND FUTURES COMMISSION	Respondent

Tribunal: Hon Mr Justice Stone, Chairman

Mr Richard John Thornhill, Member

Mr Tse Kam Keung, Member

Date of Hearing: 29 August 2006

Date of Determination: 7 September 2007

DETERMINATION

The applications

1. These are consolidated applications for review by the 3 applicants herein against SFC decisions which were communicated to the applicants within Notices of Decision dated 2 March 2006.

2. Messrs Andy Choy, Charles Cheng and George Li are all officers within that which, for immediate convenience of reference, we refer to herein as 'the Upbest Group'.

3. Upbest Group Ltd was the holding company which controlled, *inter alia*, Upbest Securities Ltd, which in 1995 was registered with the SFC as a dealer under the Securities Ordinance then in force, whilst in about October 2000 Upbest Investment Ltd was registered with the SFC as a securities margin financier under the Securities Ordinance. At the material time, both Upbest Securities and Investment were under a statutory duty to provide to the SFC certain financial information, including, at monthly intervals, their amounts of liquid capital in a financial return to be lodged with the regulator.

4. Upbest Finance Limited, whilst part of the Upbest Group, was a licensed money lender, and owed no like duty to disclose to the SFC its liquid capital provision.

5. This case essentially is about the manner in which this corporate structure, and in particular the reporting requirements under the Financial Resources Rules ('FRR'), was manipulated to the financial advantage of the Upbest Group by officers of companies within that group.

6. Mr Andy Choy, the 1st applicant herein, was the financial controller of the Group, and made daily decisions as to intra-group borrowing and lending; Mr Charles Cheng, the 2nd applicant, was a director of Upbest Group, Upbest Finance Upbest Securities and Upbest Investment, and was registered as a dealing director of Upbest Securities and Investment; and Mr George Li, the 3rd applicant, was a director of Upbest Group and Upbest Securities, and was registered as a securities dealing director of Upbest Securities, and responsible for compliance matters within the Group.

7. In substance, the specific regulatory Decisions against which the present applications are mounted are as follows:

(1) *As against the 1st applicant, Mr Andy Choy,* that his licence should be suspended for a period of nine (9) months for misconduct in that he knowingly provided false and misleading information to the SFC in that he 'window-dressed' the financial position of Upbest Securities and Upbest Investment by way of intra-group company loans, and was responsible for the failure of Upbest Investments to maintain the required level of liquid capital on 31 December 2002 and 2 January 2003, and to notify the SFC of its liquid capital deficiency;

(2) *As against the 2nd applicant, Mr Charles Cheng,* that his licence should be suspended for a period of six (6) months for misconduct in that he knew of the 'window dressing', was himself a party to the provision of false information, and was responsible for the failure of Upbest Investments to maintain the required level of liquid capital on 31 December 2002 and 2 January 2003, and to notify the SFC of its liquid capital deficiency;

(3) *As against the 3rd applicant, Mr George Li,* that his licence should be suspended for a period of four (4) months for misconduct in that he knew of the 'window dressing' and was a party to the provision of false information.

8. The applicants are aggrieved at these Decisions – hence these proceedings, which formally were commenced by letters of application for review dated 22 March 2006, to which was annexed a document intituled as 'Common Grounds of Appeal'.

The factual background

9. At this stage it may be helpful to provide a summary of the factual background which has culminated in the disciplinary sanction taken by the SFC against these three applicants.

10. Upbest Finance, a licensed money lender (it was granted its licence in 2000), functions as the finance arm of the group. This case is not about loans granted by Finance, but, to the contrary, focuses upon the accounting treatment of the repayment of loans purportedly granted *to* that company.

11. In broad terms, what happened was this: within the functioning of the Upbest group, Upbest Securities and Upbest Investment were used to provide inter-company 'loans' to Upbest Finance.

12. The significant aspect of this arrangement was that such loans were provided at a lower rate of interest in comparison with the bank rate then prevailing, these inter-company loans effectively (and, it is said, significantly) serving to reduce Upbest Finance's bank borrowing costs.

13. The nub of this case, and the disciplinary proceedings commenced consequent thereon, is the manner in which such loans, and the alleged repayment thereof, were recorded in the accounts of Upbest Securities and Upbest Investments, the result of which was to provide the SFC, *qua* regulator, with the false and misleading representation that particular loans in question in fact had been repaid, when this was not the correct position.

14. In turn this provided, via returns filed pursuant to the FRR – and this is the essence of the regulator's complaint – the SFC with an incorrect (and, it is said, a deceptively favourable) impression of the state of the lenders' (namely, Upbest Securities and Upbest Investment) liquid capital, thus preventing the regulator from making an accurate assessment as to the compliance, by Upbest Securities and Investments, with the requirements of the FRR; in fact, it is alleged that on at least two occasions this process had the effect of disguising the fact that Upbest Investments' liquid capital had fallen *below* the required minimum level.

15. The relevant transactions are larded with detail, and are helpfully summarized in the Appendices to the respective Notices of Decision issued by the SFC.

16. In outline, there were 3 primary steps within this accounting scheme:

first, transfer of funds by cheque from lender to borrower;

second, at or about the same time, the delivery of a cheque drawn on the borrower (Upbest Finance) in favour of the lender (Upbest Securities/Investment), which cheque deliberately was *not* presented to the bank for a period, but nevertheless immediately was entered into the books of Upbest Securities/Investment; and

third, at or about the same time when such cheques ultimately were presented to the bank to be encashed, the advance of a new loan from lender (Upbest Securities/Investment) to borrower (Upbest Finance) in the same or similar amount.

17. We apprehend that it was this third and final step which stimulated Mr Beresford, appearing for the SFC on these applications, to characterize this process in his address to the Tribunal as in substance constituting little more than a "cheque kiting operation".

18. We have been informed by Mr Beresford that the scheme was uncovered when the SFC reviewed the lenders' bank reconciliations in which the unpresented cheques had been subtracted from the ledger balance in order to reconcile it with the bank statement.

19. On 21 January 2003 the matter was drawn to the companies' attention at a meeting, and on 28 and 30 January 2003, the SFC wrote to Upbest Securities and Upbest Investment respectively and raised its concerns about this practice, which thereafter immediately ceased.

20. By letter dated 14 March 2003, at the request of the SFC, the true and correct liquid capital positions of Upbest Securities and Upbest Investment for agreed dates was disclosed.

21. In this connection, in his outline written submission Mr Beresford helpfully has produced a list of 'misstated FRR returns' on the part of these two companies, which for present purposes we see no need to reproduce in full.

22. To take but three examples: in February 2003 Upbest Securities filed its FRR return reporting liquid capital as at 15 May 2002 of HK$22.425 million when its actual liquid capital was HK$7.425 million; in January and February 2003, Upbest Investment filed its FRR reporting liquid capital as at 31 December 2002 of HK$15.267 million when its actual liquid capital was HK$1.67 million, below the minimum required by the FRR, and failed to notify the SFC of this fact; and in February 2003, it filed its FRR reporting liquid capital as at 2 January 2003 of HK$7.086 million when its actual liquid capital was negative HK$7.114 million, again below the minimum and unreported to the regulator.

23. The foregoing examples – and the rest of the instances proffered by Mr Beresford – are predicated upon the regulator's assertion that the scheme as was in operation between Upbest Investments on the

one hand and Securities/Finance on the other – with 'repayment' cheques entered in the books but remaining uncashed – did *not* fall within the definition of 'cash in hand' or defined 'cash equivalents' within the FRR, rule 12, although we understand that there is no suggestion that had such cheques immediately been encashed by Upbest Securities/Finance upon delivery that these instruments would not have been honoured and paid in full.

The SFC investigation and collateral criminal prosecution

24. The SFC formally began its investigation into these matters in June 2003, and during the course of this investigation the regulator interviewed all three of the applicants herein, each of whom, this Tribunal has been told, is professionally qualified in accountancy.

25. It is undisputed that the 1st applicant, Mr Choy, as the financial controller of the group, was the author of this scheme.

26. Mr Cheng, the 2nd applicant, a director of all three companies, and who was registered as a dealing director of both Upbest Securities and Finance, is said to have condoned the scheme as was put into operation, and to have signed the cheques and the FRR returns, whilst Mr Li, the 3rd applicant, who was registered as a securities dealing director of Upbest Securities, was responsible for compliance matters within the Upbest Group, and has admitted conniving in Mr Choy's scheme.

27. In addition to the conduct by the SFC of its own internal investigation, criminal proceedings also were commenced arising out of

the same subject-matter, information having been laid by an officer of the SFC on 31 December 2003.

28. Accordingly, on 2 January 2004, summonses were issued in the Eastern Magistrate's Court against both Upbest Securities and Upbest Investment pursuant to sections 56A(1)(a) of the Securities and Futures Commission Ordinance, Cap 24 [knowing provision to the SFC as to information about liquid capital false or misleading in a material particular] and against Upbest Investment pursuant to section 121AC(1) of the Securities Ordinance, Cap 333 [failure to notify the SFC of inability to comply with the FRR on 31 December 2002 and 2 January 2003 when aware of such inability in January and February 2003 respectively].

29. In addition, also on 2 January 2004, summonses were issued out of Eastern Magistracy against the three individual applicants herein, which summonses followed a like pattern to those preferred against the companies.

30. Against Mr Choy a total of 12 summonses referable to various dates were preferred, pursuant to section 56(1)(a) of the SFCO, Cap 24, regarding the provision of false information and for aiding and abetting Upbest Securities and Investment so to do; against Mr Cheng a total of 8 summonses referable to various dates, alleging consenting to or conniving in the provision of false or misleading information by Upbest Investment and Securities under the like section and section 57(1) of the SFCO; and against Mr Li a total of 3 summonses referable to different dates pursuant to the like sections, and charging consenting and conniving at the provision of false or misleading information by Upbest Securities.

31. At this stage, therefore, there existed in parallel both a regulatory investigation and a criminal prosecution, and in such circumstances it is perhaps unsurprising that at this stage negotiations should have ensued for the settlement of the same.

32. In this connection, a Statement of Facts was agreed between the SFC and the applicants for the purpose of the SFC disciplinary proceedings.

33. This Statement is attached to a letter dated 12 June 2004 from the applicants' solicitors, Jesse HY Kwok & Co., to the SFC, and has been 'confirmed' by the signatures of the 3 applicants herein for and on behalf of Upbest Securities and Upbest Investment.

34. In the context of this review application, this Statement of Facts has resonance, and we regard this as a significant document.

35. It is 8 paragraphs in length, the initial 3 paragraphs of which identify the companies and the individuals involved, and specifically confirm that at the material time both Upbest Securities and Upbest Investment were under a statutory duty to provide the Commission with certain financial information, including their amounts of liquid capital, at a monthly interval in the form of a document called a 'financial return' that each company was required to lodge with the SFC.

36. The following paragraphs record the detailed manner in which this system operated worked; we note, for example, the following précis of the admitted position within paragraph 4 of the Statement of Facts:

> "In 2000, Choy obtained the approval of Upbest Securities and Upbest Investment to regularly transfer funds from Upbest Securities to Upbest Investment and Upbest Finance and from Upbest Investment to Upbest Finance to provide funding for Upbest Finance. The transfers-out from Upbest Securities and Upbest Investment were recorded in their respective books as inter-group company loans. Cheques were drawn on the accounts of Upbest Finance and Upbest Investment for the benefit of Upbest Securities and Upbest Investment as repayment of loans. However, Upbest Securities and Upbest Investment, under the supervision and control of Choy, did not present those cheques when they were received, although Choy caused certain entries to be made on their respective books to the effect the cheques had already been deposited into their respective bank accounts. The bank account balances of Upbest Securities and Upbest Investment were taken into account in their report of their amounts of liquid capital to the Commission. When those cheques were eventually deposited a few days later, Choy caused Upbest Securities and Upbest Investment to make another round of transfers-out in almost the same amounts as those deposited as new inter-group loans."

37. There follows within this document detail of the monthly provision to the SFC of the financial returns of Upbest Securities and Upbest Investment for the respective periods of 30 April 2002 to 30 June 2002 and for 30 November 2002 to 2 January 2003, paragraph 5 of this Statement specifically admitting that:

> "…the information contained in the financial returns concerning the amounts of liquid capital of Upbest Securities as at 30 April 2002, 15 May 2002 and 30 June 2002 and Upbest Investment as at 30 November 2002, 31 December 2002 and 2 January 2003 was false in a material particular."

38. Details of the differential between the apparent liquid capital of Upbest Securities and Upbest Investment at these dates are provided at paragraph 6 of the Statement, whilst paragraph 7 thereof recounts that "on 31 December 2002 and 2 January 2003 Upbest Investment did not have

sufficient capital as required by law", a fact only subsequently reported to the Commission by letter dated 14 March 2003.

39. Finally, paragraph 8 of this document admits:

> "Cheng knew what Choy was doing but failed to stop Choy. Despite his duties on compliance matters, Li did nothing to stop Choy but connived in what he was doing."

40. We have been told by counsel for the SFC that this Statement of Facts, as agreed for the specific purpose of the SFC disciplinary proceedings, essentially was the same as the statement of facts as was read to the Magistrate's Court in the criminal proceedings on 14 June 2004 when the 1st applicant herein, Mr Andy Choy, and Upbest Investment, were convicted on a plea of three counts of knowingly providing false and misleading information to the SFC contrary to section 56A(1)(a) of the Securities and Futures Commission Ordinance, Cap 24, whilst Upbest Investment was convicted on a plea of failure to notify the SFC of its inability to comply with the FRR contrary to section 121AC(1) of the Securities Ordinance, Cap 333.

41. As to penalty thus imposed in the Magistrate's Court, Mr Choy was fined $2000 on each summons, and Upbest Investment was fined $5,000 on each summons, and ordered to pay costs.

42. Consequent upon the guilty pleas, on the basis that the SFC would proceed on a disciplinary basis only, the SFC offered no evidence against Mr Charles Cheng on 6 summonses for offences contrary to ss 56A(1)(a), Cap 24, and s 89, Cap 221; against Mr Andy Choy on

9 summonses for offences contrary to s 56A(1) and s 89, Cap 221; against Mr George Li on 3 summonses for offences contrary to ss 56A(1)(a) and 57(1), Cap 24; and against Upbest Securities on 3 summonses for offences contrary to s 56(1)(a), Cap 24.

43. Subsequent to these events, the SFC commenced disciplinary proceedings against the applicants herein by Letters of Mindedness dated 23 March 2005, to which representations were made on behalf of the applicants dated 7 May 2005 and 3 October 2005, which process culminated in Notices of Decision dated 2 March 2006, against which Decisions these consolidated applications for review now are mounted.

The applicants' argument

44. Mr Jonathan Harris SC, appearing for all the applicants, put his case on the following broad basis:

(1) that the breach of the Financial Resources Rules (FRR) was "purely technical" in nature;

(2) that in making its Decisions in respect of these applicants the SFC had been wrong to infer that there had been a *conscious* attempt to present misleading accounts; in particular, there had been no suggestion that the scheme which had been put in place (he termed it 'the Arrangement') was necessary in order to enable the relevant companies to meet the liquidity requirements specified in the FRR; and

(3) that in any event, the penalties imposed were and are manifestly excessive.

45. Thus was two-pronged attack mounted by the applicants in terms both of liability and sentence.

46. The nub of Mr Harris' argument is contained in his assertion that on the part of his clients there had been no conscious breach of the FRR.

47. In this connection the basic theme of Mr Harris' address was that the SFC had been wrong and fundamentally in error to draw the necessary implication that in acting as they did the applicants had been acting dishonestly.

48. In this connection he cited in particular extracts from the SFC Decision of 2 March 2006, in respect of Mr Cheng wherein there appear the following passages:

at *para 19*:

> "…as long as a scheme or an arrangement has the intention and effect of concealing the true financial position of a broker firm, this constitutes window dressing irrespective of whether the liquid capital of the firm was sufficient or not. You still engaged in accounting fraud which seriously calls into question your honesty"…

and at *para 27*:

> "We believe that Choy was dishonest in devising the scheme. Upbest Investment was likewise culpable and had already admitted to knowingly providing false and misleading information to the SFC…"

and at *para 29.1 and 29.2*:

> "…we maintain our view that you were dishonest in endorsing the Scheme…With your [professional knowledge to recognize

> that the Scheme window-dressed the liquid capital position of Upbest Securities and Upbest Investment. By signing on the FRR returns in question, you had a duty to ensure that the contents of the returns were true and accurate…
>
> You signed the Brief Facts admitting that you knew what Choy had been doing but you had failed to stop Choy…
>
> Your claim that you 'honestly believed that the practice was proper' cannot be reconciled with [the facts]"

and at *para 32.6*:

> "Even though there was no liquid capital deficiency, you devised a dishonest scheme to inflate the real liquid capital position of Upbest Securities and Upbest Investment".

49. Mr Harris submitted that there was no "direct evidence" that Cheng or Li, or for that matter Choy (leaving to one side the fact of the plea bargain in the criminal proceedings) had introduced the scheme in question as the consequence of a conscious decision to include figures in the FRR return which had resulted in an inflation of the liquid assets of Upbest Securities and Investment, and thus that this inference as drawn by the regulator was drawn "without any apparent regard to the law relating to when inferences can properly be drawn."

50. In terms of the drawing of inferences, Mr Harris noted that section 218(7) of the Securities and Futures Ordinance, Cap 571 expressly provides that the standard of proof by which any question or issue before the SFAT is to be decided is the civil standard, that is, upon the balance of probabilities, and cited the SFAT Determination in *Application 6 of 2004* in which the Tribunal quoted from and accepted the formulation in Lord Nicholl's seminal judgment in *In re H (Minors) [1996] AC 563 at 586E* that:

> "when assessing the probabilities the court will have in mind as a factor, to whatever extent is appropriate in a 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…"

51. With this benchmark in mind, Mr Harris observed that the allegations as made against the applicants were serious, with dishonesty being suggested and found, and that consistent with established principle the evidence required to prove dishonesty must be strong, and that an inference of dishonesty should be drawn only in a very clear case. He suggested, further, that parallels could be drawn from the statements on the subject of Insider Dealing Tribunals, where the position consistently had been adopted that an inference of dishonesty could be drawn if it was "the only inference which could be drawn from the established facts", and he submitted that this was the correct test to be applied in the present case.

52. The focus of Mr Harris' argument was that the only facts to be incontrovertibly established was that 'the Arrangement' was consciously formulated and introduced, and that there was no direct evidence of a dishonest design "in the sense of a conscious intention improperly to circumvent the FRR's" lying behind the Arrangement's formulation or introduction; to the contrary, he said, the SFC simply had *assumed* that the Arrangement was dishonestly introduced.

53. Mr Harris observed that the SFC neither had explained nor justified its view as to dishonesty against the undisputed fact that the Arrangement saved the Upbest Group the sum of HK$400,000 in interest in 3 months, so that there had been, as he put it, "a genuine commercial

benefit to the Upbest Group in introducing the Arrangement which had nothing to do with compliance or otherwise with the FRR's", and indeed that this was the reason proffered by the applicants when they had been interviewed on the subject by the SFC.

54. Moreover, Mr Harris argued, the Arrangement clearly was not necessary in order to ensure that the liquid asset requirements of the FRR's in fact were met: these cheques could have been honoured if they had been presented, and the SFC never had suggested that, if presented, they would not have been met.

55. Nor, he said, had there been any attempt to conceal the situation. The Arrangement had been obvious from the accounting records and reconciliation statements of Securities and Investments, and in fact had been going on for some time; moreover, the financial statements had been audited without objection, and the books of Securities and Investments had been inspected prior to the SFC investigation by the Intermediaries Supervision Department of the SFC, with the Arrangement not having been queried at that time.

56. Looked at in the round, therefore, he strongly submitted that on the evidence the SFC could not properly have found that the Arrangement had been introduced in order to circumvent the FRR's, and the regulator should have found that there had been a mere "technical breach" of the FRR's, and assessed its penalties accordingly.

57. As a matter of fact, he asserted, it was "far more probable" that objective consideration of the facts of this case would lead to the

conclusion that the Arrangement was introduced in order to save interest (as in fact had been the case), than with the intention of circumventing the FRR's. It was clear, he said, that the interest rate the Wing Hang Bank charged Upbest Securities and Investments on their credit facilities was lower than the bank facility as was charged to Finance, and the reason it was worth using the facilities was that Upbest Finance could lend money to clients at a higher rate of interest than Securities and Investments paid on their borrowings.

58. Nor was there any dispute – indeed, it was common ground – that the Arrangement had been formulated by Mr Choy, although Messrs Cheng and Li had been told of the Arrangement, and admittedly had approved its use. A large sum in interest had been saved for the Group, there never had been any reason why the cheques could not have been honoured when presented, and, as Mr Harris disarmingly put it, "the timing of the presentation was entirely a matter of commercial judgment".

Decision

59. We have taken some care to set out on some detail the applicants' argument upon the 'dishonesty issue'.

60. We have done so because we feel bound to observe that we find it surprising in the circumstances that this case has been portrayed thus. A good deal has been said about 'window dressing' in terms of the FRR's; our view is that the applicants' argument in this case itself has been persuasively 'window dressed' so that, in substance, the very matters of which the regulator was entirely right to have been concerned have in

effect have been portrayed as little more than an inconsequential ‘technical breach’.

61. We do *not* accept this characterization.

62. In fact, the greater the degree of reflection, the more resistant Tribunal has become to the submissions as to primary liability which have been advanced on the applicants’ behalf.

63. The hard, and inescapable, facts underpinning this case are as follows:

(1) the three applicants are all accountancy professionals;

(2) an ‘arrangement’ or ‘scheme’, call it what you will, in the form described herein, was put into place at the instigation of Mr Andy Choy, with the connivance/condonation of Messrs Cheng and Li, to file FRR returns which, on any basis, patently did *not* reflect the true and accurate liquidity position of Upbest Securities and Investments;

(3) to the contrary, such returns reflected a false and intrinsically misleading picture, as indeed has been admitted; in this regard we agree with and accept the contention of Mr Beresford, for the SFC – who conducted this application in his usual sensible and balanced fashion – that there can be no dispute in principle that an uncleared/unpresented cheque does *not* fall within the rubric of ‘cash in hand’, and that under generally accepted accounting principles only cheques held in the ordinary course of collection fall within the meaning of ‘cash equivalent’. Accordingly, when (as in this case) cheques

specifically were held back from presentation so as to give the borrower extended use of the funds, to purport to treat such as 'cash' is not in accordance with generally accepted accounting principles, and thus is outwith the requirements of FRR, Rule 4, which provides that a registered person shall calculate all assets and liabilities in accordance with generally accepted accounting principles unless otherwise specified, and that he shall account for all assets and liabilities in such a way "as recognizes the substance of the transaction";

(4) in the agreed Statement of Facts each of the applicants has *admitted* the falsity of information contained in the financial returns for specified dates – see paragraph 5 of the Statement of Facts, at paragraph 37, *infra* – and have accepted that the accounting treatment/system was wrong, and further that Messrs Cheng and Li knew what Choy was doing but failed to prevent this occurring.

64. Against this background the objective observer might think that the argument as now sought to be run by these applicants in this review application was ambitious to say the least, not least since none of these three gentlemen were inclined to go into the witness box in order to buttress the primary argument as to the absence of a dishonest and wholly disingenuous design.

65. In our view, on the present state of the evidence and the admissions as made (the case was argued on the papers, with no *viva voce* evidence being presented before us), there can be little doubt but that these applicants well knew and appreciated that the FRR returns to the SFC of

Upbest Securities and Upbest Investments contained false representations in light of the bookkeeping treatment as was accorded to the 'repayment' cheques within the accounts of these two companies, which to the third party regulator represented that cash was in the lending company and not in the borrowing company – that is, that the cheques had been deposited into the lending company's account *as at the date of* the unpresented cheques, when patently this was not the situation – these cheques, for collateral commercial purpose, deliberately and calculatingly having remained *unpresented.*

66. As Mr Beresford has pointed out in some detail in his skeleton argument – primary facts which cannot be gainsaid – the clear and false representation in the books of Upbest Securities and Upbest Investment was that the loans had been 'repaid' by Finance, and thus that the cash was back in the lending company; moreover, it also appeared from the borrower's books that the cash in question had been returned to the lender (even though the borrower, Finance, was, on the applicants' case, using such cash to fund its loans to clients).

67. We accept the regulator's argument that the applicants knew that these representations were false because they knew that by reason of this scheme or 'arrangement' the borrowing company had retained use of the funds; as Mr Beresford has highlighted, the applicants' admitted intent was for the borrowing company to have use of the lending company's cash for the period in which presentation of the relevant cheques was withheld. We further accept the proposition that even when repayment in fact occurred, this was nothing more than that which Mr Beresford aptly termed a "conduit pipe", because as soon as the borrower's (Finance's)

cheques actually were presented, the lender (be it Securities or Investment) immediately had lent the same or substantially the same amount.

68. Viewed thus, therefore, we are unable to accede to the argument that in the situation prevailing no irresistible inference should be drawn of 'dishonesty' on the part of the applicants herein, albeit if such inference were to be necessary, we should not hesitate to draw it. In the particular circumstances, however, and not least in light of the admitted facts, we do not consider that the drawing of inferences should be a consideration which ought to weigh on our minds, nor to provide any obstacle in our evaluation of this case.

69. It seems to us that these applicants cannot have it both ways. They cannot on the one hand admit the falsity of the details within the returns as provided to the regulator, yet on the other seek to disavow any dishonest intent thus to mislead; in this connection we take the view that 'motive' does not negate such intent, but serves only to mitigate – the fact that there may have been a 'genuine commercial' reason for doing what was done does *not* serve to validate the dishonest methods used to achieve such arrangement.

70. On the evidence these applicants clearly knew, by reason of a scheme which depended for its collateral financial advantage upon the non-presentation of cheques held by Upbest Securities and Investment, that the inevitable consequence would be falsely to represent and to mislead the regulator as to the apparent state of the liquidity of those companies, and hence obviate the need to take appropriate action in the event (and in the case of Upbest Investment this occurred on at least two occasions) that a

lending company's capital had fallen below the required minimum; in this context we further accept the proposition that if the SFC was satisfied that the applicants knew of the falsity of the representations contained within the accounting entries, such representations properly were characterized as 'dishonest', and that it was entirely open for the SFC to come to this conclusion upon these facts.

71. We accept, of course, that in principle, the existence of a dishonest state of mind can be negated by an honest and reasonable belief in the existence of circumstances which, *if* true, would make the impugned act innocent, and it is in this context we appreciate that the claim is made that the applicants believed that they were entitled to treat the unpresented cheques as 'cash', thus justifying the accounting treatment of such cheques.

72. In the prevailing circumstances however, this argument strikes us as thoroughly disingenuous, and insofar as it continues to be pressed upon the Tribunal, we have no hesitation in accepting the submission that a claim to such belief is unreasonable to the point of being absurd; accordingly, we find that the regulator was perfectly entitled, as it did, to reject this explanation.

73. In accounting terms these three gentlemen most certainly were not inexperienced *naifs*; in this connection we bear specifically in mind their education and professional training, the formal admissions made in the Statement of Facts made for the purpose of the disciplinary proceedings, and the admitted facts underlying the guilty pleas of Mr Choy and of Upbest Investment in the Magistrate's Court.

74. We find it curious that the financial advantage in terms of interest savings accruing from adoption of this scheme is a factor which now is positively trumpeted by these applicants as justification for their actions – thereby buttressing the correlative argument that, since there was little doubt that the cheques, if presented, would be honoured, such breaches of the FRR should be considered as mere ‘technical’ offences.

75. The stark submission as now made, in effect, is that manipulation and presentation of misleading accounts which serve to obscure, or to present a false and misleading impression of the true liquidity position of the registered companies, is justified by what thereby was achieved in the form of substantial collateral commercial advantage, given that in fact there was no underlying liquidity difficulty.

76. We are wholly unimpressed by this approach. This does the applicants no service, and in our view serves to highlight an apparent disdain and lack of respect not only for accurate compliance with the Financial Resources Rules, but also for the market integrity that these Rules seek to engender.

77. If and insofar as such needs to be expressly stated – and from the facts and arguments in this application it seems to be the case that it does – there should be no doubt but that this Tribunal does *not* share such apparent disregard for the importance of the FRR, and the necessity for accurate and truthful returns/submissions thereunder.

78. In terms of maintaining market integrity, a minimum capital requirement serves a number of important purposes, not least amongst

them being that it fosters confidence in the financial markets and in the participants therein, and that it also assists the market regulator to assess the financial status, and thus the fitness and properness, of a licensed corporation; an accurate return, under the FRR, may even act as an 'early warning' to a market regulator, enabling action to be taken to preclude investor loss, which we should have thought was a consideration likely to be uppermost in any regulator's mind.

79. Thus, FRR rule 35 required Upbest Securities and Investment, in common with all other registered companies, to file monthly FRR returns with the SFC, including a computation of each company's liquid capital; as we have seen, however, those in charge of the reporting requirements of these two companies took the view that factually incorrect and misleading returns should be filed for no justification other than to feather their own commercial nest, which is as poor (and unconvincing) an example of special pleading as we have encountered.

80. We wholly disagree with the submission made by Mr Harris (*vide* para 5.1 of his skeleton argument) that "the Arrangement …did not cause the FRR's to be breached" and further that (at para 5.3) it is not possible to infer that the applicants deliberately circumvented the FRR's and "consciously window dressed Securities and Investment accounts."

81. The evidence is overwhelming the other way. It is as plain as a pikestaff that the arrangement caused a breach of the FRR's, and that the applicants well knew that it did; to the contrary, it is not conceivable that they believed that the returns presented to the SFC presented a true and accurate picture of the liquidity situation.

82. On the material before us, our firm conclusion is that the relevant accounts were presented well knowing that they provided the appearance of compliance, when in fact the cheques in question could not, as in our judgment the applicants well knew, properly be treated as 'cash in hand'.

83. Nor is the fact that, as Mr Harris has stressed, "there was never any reason to doubt that the cheques would be honoured when presented" to the point.

84. The regulator is entitled to expect, indeed to *demand*, true and accurate submissions returns made pursuant to the FRR; whether or not under the scheme in place in this instance these cheques *in fact* were good, and if presented would have been honoured, is not a matter upon which the regulator, had it known the true situation, would have been in a position to make any judgment, which is precisely why it is essential that returns made pursuant to the FRR should be true and accurate – on any basis demonstrably not the situation in the present case.

85. In our judgment the SFC was entitled to take the view that it did in this case, and to reject the view that mere 'technical breach' of the FRR were involved, and we reject as firmly as we may the submission on behalf of the applicants that all that these events merited was a slap on the metaphorical financial wrist.

86. It is to the issue of the appropriate penalty that we now turn.

Review of the penalties imposed

87. As noted at the outset, the penalties imposed upon the applicants by the regulator were 9 months suspension in the case of Mr Choy, 6 months in the case of Mr Cheng, and 4 months in the case of Mr Li.

88. The submission as to sentence by Mr Harris was, of course, predicated upon the success of his critique of the SFC approach toward his clients, so that were he to have been successful (which he has not) in terms of his primary contention that the SFC should have approached the assessment of penalty on the basis of a mere 'technical' breach of the FRR, then it followed that the sentences in fact imposed, on a different basis, would have substantially to be recast, in which connection Mr Harris trailed his coat on imposition of a public reprimand and/or a monetary penalty; as to the latter, he suggested a 'voluntary payment' of HK$250,000, given that at the time of these offences there existed no jurisdiction to impose a fine.

89. In light of our rejection of his primary case – our unequivocal view is that this was a thoroughly disingenuous and commercially self-serving scheme which had the practical effect of positively misleading the regulator as to the true liquidity position of Upbest Investment and Securities – the applicants' position as to sentence is correspondingly weakened.

90. In this regard we apprehend that Mr Harris' secondary submission was that even *if* the Tribunal were to accept the SFC view as to

the existence of dishonesty in terms of the FRR returns as were in fact filed during the pendency of this ‘arrangement’, nevertheless the suspensions as were imposed were excessive in the particular circumstances, albeit counsel clearly accepted, as he had to, that his scope for argument in this regard was greatly circumscribed.

91. We have accorded this aspect of the case some reflection, and we confess that we have not found it easy to strike what we consider to be the right balance. We have also attempted, we trust successfully, to put out of our minds the irritation we have felt in considering the manifest lack of merit of the applicants’ primary case.

92. At the end of the day we have come to the conclusion, albeit not without a degree of hesitation, that whilst in our view the SFC has been correct in principle in the imposition of suspensions, nevertheless we have been unable to shake off the impression that the regulator has ‘over-egged’ the pudding somewhat in terms of the length of such suspensions, although we understand how and why this should have come about, given the history of this case.

93. Nevertheless we take the view that in the particular circumstances, wherein there was no investor risk and no loss was caused, and in light of the clear records of these applicants, together with the fact that this is *not* a case wherein the true liquidity position was obscured because the corporate entities involved *in fact* were unable to make the liquidity requirement – as we have observed, there seems to be no suggestion that should the cheques in question immediately have been presented that they would have been dishonoured – that there is some

scope for a reduction in the term of the suspensions as handed down, albeit we wish to make it clear that we are wholly uninterested in any form of 'voluntary payment' of the type tentatively canvassed by counsel for the applicants; we take the view that in a situation such as this any possible monetary resolution is, and would be, entirely a matter between the regulator and the applicants.

94. It strikes us, also, that if and in so far as motive has any impact or relevance in this case, such should be factored into the case *solely* within the context of sentence.

95. Accordingly if, which has *not* been disputed – Mr Beresford specifically and very obviously declined to make any submission as to motive – the reason underpinning this scheme was to lock into a more favourable interest rate regime, it seems to us that absence of inherent venality, in the sense of an overriding intent to deceive the regulator as to *actual* illiquidity of a registered corporation, is an element which perhaps has not been accorded sufficient weight within the discretionary 'mix' in terms of appropriate sentence.

96. We repeat that we attach importance to the integrity of the FRR's, and to the regulator's ability to trust and to rely upon the returns submitted pursuant thereto, and we accept that this is not a case in which a monetary penalty or a public reprimand would be sufficient, and that periods of suspension indeed are required, not least to send the appropriate message to the market in terms of compliance with the FRR.

97. We would add, also, that we have not gained material assistance from other cases involving non-compliance with the FRR's; as generally is the position, each case stands, or falls, on its own very particular facts.

98. In all the circumstances, however, in the exercise of our discretion we have decided to vary the periods of suspension respectively handed down to these applicants, and in substitution therefor we have determined as follows:

(i) that the period of suspension imposed upon the 1st applicant herein, Mr Andy Choy Ye King, be reduced from 9 months to 6 months;

(ii) that the period of suspension imposed upon the 2nd applicant herein, Mr Charles Cheng Kai Ming, be reduced from 6 months to 4 months;

(iii) that the period of suspension imposed on the 3rd applicant herein, Mr George Li Kwok Cheung, be reduced from 4 months to 3 months.

99. In our judgment, such reduction in penalty more appropriately reflects that which we perceive to be the inherent justice of the situation in all the circumstances of this case.

Order

100. It follows from the foregoing that in this application the Order of this Tribunal is as follows:

(1) Save that the periods of suspension imposed upon the 1st, 2nd and 3rd applicants herein be varied, and there be substituted therefor the periods of suspension specified in paragraph 97 herein, the consolidated applications for review herein be dismissed;

(2) That each of the periods of suspension, as now varied, do commence upon the expiry of the *third* day following the date of publication this Determination.

101. As to costs of this consolidated application, we make an order *nisi*, such order to become absolute within 21 days from the date of this Determination if no written representations be received as to such costs' order, that 80% of the costs of and incurred by these review applications be paid by the applicants herein, such costs to be taxed if not agreed.

102. Notwithstanding that the applicants ultimately have succeeded in obtaining a reduction in the respective periods of suspension, we take the view that this is the appropriate costs/order in light of all the circumstances of this case, wherein the requirements of the FRR and the accuracy of the returns thereunder knowingly were flouted purely for collateral commercial advantage, and wherein the principal argument mounted on this Determination on behalf of these applicants has been decisively rejected.

Finally

103. This Tribunal regrets the significant amount of time which has been taken to render its Determination in this case. In this regard the

Chairman wishes to state that this unfortunate delay is solely his responsibility.

Hon Mr Justice Stone (Chairman)	Mr Richard John Thornhill (Member)	Mr Tse Kam Keung (Member)

Mr Jonathan Harris SC, instructed by Messrs Robertsons, for the Applicants

Mr Roger Beresford, instructed by the SFC, for the Respondent