Application No. 5 of 2004

IN THE SECURITIES AND FUTURES APPEALS TRIBUNAL

IN THE MATTER OF Section 23 of the Securities and Futures Commission Ordinance (Cap. 24) and Section 56 of the Securities Ordinance (Cap. 333)

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

AND IN THE MATTER OF an application for review by ANDREW JOHN PEREGRINE KORNER

BETWEEN

ANDREW JOHN PEREGRINE KORNER Applicant

and

SECURITIES AND FUTURES COMMISSION Respondent

Tribunal: Hon Mr Justice Stone, Chairman

Date of Hearing: 6 July 2004

Date of Determination: 23 July 2004

DETERMINATION

The Application

1. This is an application by Mr Andrew John Peregrine Korner against a decision of the Securities and Futures Commission ("SFC") dated 29 March 2004 whereby Mr Korner's licence as a securities investment adviser was suspended for 6 months pursuant to the provisions of section 56 of the Securities Ordinance, Cap. 333.

2. The powers of the SFC under section 56 of the Securities Ordinance, now repealed, remain exercisable after 1 April 2003 pursuant to section 64, Schedule 10, Part 1 of the Securities and Futures Ordinance, Cap. 571.

3. The basis of the decision of the SFC, as communicated to Mr Korner in its Notice of Decision, was essentially two-fold:

> *first*, that the company of which Mr Korner was the sole investment advisor director, Asian Capital Partners (HK) Ltd. ("ACPHK") had been in breach of the then

applicable Financial Resources Rules ("FRR") for a period between 2001 and 7 April 2003, in that during that period it had failed to maintain the required level of net tangible assets of HK$500,000, that it had failed to notify the SFC in writing when such assets fell below this requirement, and that it had failed to file its annual returns and audited financial statements in time, and that Mr Korner, as the director responsible for daily operation and management, bore a significant amount of responsibility for such regulatory breaches; and

second, that Mr Korner personally lacked financial integrity in that he had acted to the detriment of erstwhile employees of ACPHK by attempting to shield ACPHK, and other companies active within the Asian Capital Partners Group, from legitimate financial claims of such employees, and had failed to honour Labour Tribunal settlement agreements reached with these employees.

4. As a consequence of these findings, the SFC concluded that Mr Korner's fitness and properness to act had been called into

question, hence the 6 month licence suspension initially the subject of these proceedings.

5. Mr Korner has taken issue with this decision, and, with the consent of the parties, this review has been conducted before this Tribunal consisting of the Chairman sitting alone, pursuant to the provisions of section 31, Schedule 8, Securities and Futures Ordinance, Cap. 571.

Pre-hearing variation by the SFC

6. The foregoing summarises the situation as it existed on the papers at the time of the filing, on 20 April 2004, of Mr Korner's application for review of the SFC decision of 29 March 2004.

7. However, by letter dated 17 June 2004 from Ms Victoria Williams, Associate Director of Enforcement of the SFC, the SFC informed this tribunal that the regulator had decided to *withdraw* its finding that Mr Korner personally lacked financial integrity, and thus that the only issue before the tribunal upon the hearing of Mr Korner's application was the appropriate penalty to be imposed upon Mr Korner for his responsibility for the failure of

ACPHK to comply with the FRR and the associated reporting breaches.

8. This letter pointedly did not suggest the penalty that the SFC now considered appropriate. However, in the skeleton argument filed on 30 June 2004 prepared by Mr Adrian Bell, counsel for the SFC, the tribunal was specifically asked *not* to uphold the finding of a personal lack of financial integrity, although it was asked to uphold what may be termed the 'FRR findings' made by the SFC – which breaches had been admitted by Mr Korner – the submission therein being that the appropriate sanction for such breaches was a licence suspension of 2 months.

9. Hence, the parameters of this review had changed, and changed significantly.

The Argument

10. The result of this alteration in SFC stance was that the argument upon this application was confined to a debate as to the penalty appropriate for breaches of the FRR in force at the date of the admitted infractions.

11. In this connection it is worth noting that such FRR had undergone a substantial change consequent upon the coming into force, on 1 April 2003, of amending legislation in the form of the Securities and Futures Ordinance, Cap. 571. New FRR requirements were laid down therein, whereby a new 'liquid capital requirement' was to replace the previous 'net tangible assets' requirement, and a lower capital floor was established for advisers subject to the specific licensing condition that it should not hold client assets. Thus, for an investment adviser in the position of ACPHK, which it is common ground handled no such assets, this statutory requirement was reduced from HK$500,000 to HK$100,000, albeit at the date of the regulatory breaches the subject of this review, the higher figure remained in force.

12. At the core of Mr Harvey's submission on behalf of Mr Korner was that his client found himself in a curious, if not invidious position. Having been specifically found by the regulator to be lacking in financial integrity – which finding, he said, must have been the principal 'driver' of the suspension of 6 months as originally imposed – the applicant found himself in the position of having to submit its skeleton argument without having a target at which to aim. In any event, now that it was clear that the penalty sought to be upheld was a 2 month suspension, Mr

Harvey submitted that the sanction proposed was disproportionate and excessive in light of Mr Korner's conduct and the fact that the admitted breach, accepted by the SFC to be neither deliberate nor willful, had been "self reported", and that in the circumstances there was no question of third party assets having been put at risk.

13. Mr Harvey noted, further, that Mr Korner had engaged in a lengthy correspondence with the SFC as to the ongoing financial status of ACPHK and the likely time at which, and the means whereby, that company might be restored to full compliance with the FRR and the associated filing requirements. Additionally, he said, Mr Korner deeply regretted the occurrence of the breaches and fully appreciated the significance of the FRR; indeed, shortly after the breaches had been discovered and reported, the company had confirmed, through Mr Korner, that it would not carry out the business for which it was registered under the Securities Ordinance until it was again in compliance with the FRR.

14. For the SFC, Mr Bell underscored the importance of the FRR, and suggested that in fact it was the breaches of these requirements, and not the issue relating to the disaffected ACP Group employees, which was the thrust of the SFC disciplinary action. He submitted that whilst Mr Korner indeed had brought

these breaches to light, this had occurred only because of an SFC inspection into the affairs of ACPHK which had been stimulated by the employees' complaints, and it appeared that until this inspection was imminent Mr Korner, as the guiding mind of the company, had been negligently unaware of the breaches of which complaint was made.

15. Mr Bell further emphasized the continuous nature of the breach of the liquidity requirements, from a date uncertain in 2001 to the date of rectification in April 2003, and also noted the delay in such rectification notwithstanding regular SFC requests to put the company's house in order, which in fact had been done by an infusion of capital consequent upon the remortgage by Mr Korner of his London property. In addition, Mr Bell noted that the breach of the requirement to notify the SFC in writing when the net tangible assets of the company had fallen below the legal requirement was a breach continuing from 2001 to 26 November 2002, the latter being the date of a letter furnished by Mr Korner to the SFC at the meeting with the regulator on that date, whilst the audited financial statements of ACPHK to 31 March 2001 should have been submitted on 1 February 2002, but were not submitted until 12 December 2002.

16. Looked at in the round, said Mr Bell, and bearing in mind the regulatory importance of FRR, the breach of which, together with the associated reporting breaches, had continued for a substantial period undoubtedly as the result of the applicant's negligence or incompetence, a licence suspension of two months was entirely appropriate. Accordingly, he submitted, this should not be a matter with which this tribunal should be persuaded to interfere.

Determination

17. This tribunal has stated on a number of previous occasions that as a matter of general principle it is reluctant to interfere with the decision of the regulator in the field unless the applicant seeking a variation in disciplinary penalty successfully shoulders the burden of demonstrating that something has gone substantially wrong, and accordingly that the particular decision should not be permitted to stand.

18. Each case obviously depends upon its particular facts, and in my view the circumstances of this particular case are very much out of the ordinary. In a real sense, of course, the regulator already has acknowledged that something is amiss. It must be rare indeed when the SFC of its own volition chooses subsequently to

change the penalty formally handed down in its Notice of Decision – in this instance reducing the licence suspension by two thirds, from 6 months to 2 months – and in the process *abandoning* that which cannot conceivably be other than the most damning finding against Mr Korner, both personally and *qua* investment adviser, namely a personal lack of financial integrity. Reputations are hard won and easily lost, and it deserves to be stressed in this Determination that this 'finding', as originally made by the regulator, no longer stands.

19. The circumstances in which such withdrawal occurred are less than clear. Certainly Ms Williams' letter of 17 June (paragraph 7 refers) does not enlighten. Mr Harvey suggested that the regulator was minded to re-think its position after sighting the affidavit filed by Mr Korner, on 8 April 2004, which dealt primarily with the disputes of the disgruntled former employees of the ACP Group, the allegations made against him in terms of the 'shielding' of their claims from ACPHK and other group companies, and the alleged failure to honour settlement agreements. I am told that Mr Korner was advised to file this affidavit, which it had been intended to place before this tribunal had this allegation been persisted in, because he had never been interviewed by the SFC about this issue, and thus he had taken the opportunity to

repeat on oath his version of events as given in earlier written responses to the SFC. For his part Mr Bell, whom in this application has said all that could reasonably be said on behalf of his client, in commenting upon the regulator's change of stance alluded to certain observations made by this tribunal during the directions hearing for this application.

20. Whatever the true reason for the current position, however, in the circumstances of this case I am disinclined to accept at face value Mr Bell's submission that throughout the SFC investigation into ACPHK that the *primary* focus had been on the breach of the FRR and the associated reporting requirements. I understand the forensic attraction of that submission by counsel seeking to uphold the current substitute proposal for a 2 month suspension, but in my view such submission is unlikely to reflect the reality of the situation. On the SFC's own documents this inquiry initially "stemmed from complaints" by the disaffected employees, it was those complaints that ACPHK was in financial difficulty (as clearly was the case, Mr Korner apparently having paid some of the employees from his own pocket) which had precipitated the initial meeting between Mr Korner and SFC staff on 26 November 2002, and it was those complaints which patently underpinned the erstwhile 'finding' as to Mr Korner's personal

lack of financial integrity, as outlined in the SFC Notice of Decision and Statement of Reasons dated 29 March 2004. Against this backdrop, and the significant reduction in the penalty as now proposed, it strikes me as somewhat ambitious seriously to suggest that the breaches of the FRR had represented the dominant concern throughout.

21. Be that as it may. Do these breaches of the FRR, and the associated reporting omissions merit the alternative penalty of a 2 month suspension as is now mooted?

22. I have difficulty in accepting this proposition. In principle I do not doubt the importance of compliance with FRR, although I observe in passing that the concern as to compliance assumes a significantly greater profile in situations in which the transgressor holds client assets – a situation which on its face appears to have been specifically recognized by the legislature in significantly downgrading the FRR requirement from HK$500,000 to HK$100,000 in the circumstance of an investment adviser such as ACPHK holding no client assets.

23. It is common ground in this case that ACPHK is to be the subject of a public reprimand, albeit a reprimand not yet

formally issued pending the result of this application, and from which decision there is no appeal. In the particular circumstances – and I stress that each case stands or falls on its own facts – I fail to understand why Mr Korner's actions should merit any greater punishment. It seems tolerably clear that the now-abandoned penalty of suspension for 6 months has influenced the choice of the period of 2 months as currently mooted, although in my judgment, on the basis of the papers before the tribunal, the SFC has been entirely correct to retreat from, and to disavow, its original position; in this context it seems fair to observe that the case originally mounted against Mr Korner, involving the serious assertions as to his lack of good faith and lack of financial integrity – which assertions appear to have resulted from the unsubstantiated complaints of disgruntled employees of APCHK sister companies Renomate and Modern State – does not represent the SFC's finest hour.

24. On any basis the admitted FRR defalcations in this case tend very much to the lower end of the fault spectrum. As Mr Korner had pointed out in his written responses to the SFC, ACPHK was an operationally inactive company which had not been engaged in any ACP group investment banking transactions since 1999, it neither had clients nor employees, and the great

majority of ACP group clients, their transaction counterparties and the markets of execution for their transactions had been outside Hong Kong. Mr Korner had admitted the infractions, which had come to his attention and of which he had informed the SFC, and he had undertaken both to remedy the resources requirement and not to permit ACPHK to do business again until such infraction was remedied.

25. I understand the SFC complaint about the length of time taken to infuse capital into ACPHK – in the event achieved not through the culmination of a business deal but by the remortgaging of Mr Korner's London house – and I appreciate the regulator's assertion that both he and ACPHK were negligent (as opposed to deliberate and wilful, which is not suggested) in failing to detect and report the FRR breach, although in this context I factor also into the 'mix' that Mr Korner's admitted failure to discover the true situation, together with the late filing of audited financial statements and annual returns, was at the least contributed to by the departure of key accounting staff from the ACP group.

26. Looking at the matter in the round there is something to be said for Mr Harvey's submission that his client has "suffered enough", and that in light of the forthcoming public reprimand to

be visited upon ACPHK, a company identified throughout the market with Mr Korner personally, that his client should not now be visited with any penalty whatever. It seems to me, however, that this plea, whilst understandable, somewhat over-eggs the pudding, and in any event this argument remains as relevant, and perhaps is of more practical consequence, in the context of the costs order in this case.

27. In normal course the tribunal would be requested to confirm or to vary the penalty imposed by the SFC, but in this unusual case the penalty initially imposed has been withdrawn, with the result that the matter remains effectively at large.

28. After some reflection I have concluded that the appropriate penalty for the infractions that remain at issue – namely the failure to maintain the required level of net tangible assets between 2001 and 7 April 2003, the failure to notify the SFC in writing of this fact, and the failure timeously to file annual returns and audited financial statements - should attract the penalty of a public reprimand. I so order.

Costs

29. I have earlier alluded to the issue of costs, which has been canvassed by counsel before the tribunal, albeit without the advantage of the parties being aware of the result of this application nor of the reasons therefor. I have agreed with counsel on both sides that I will make what is in effect a costs order *nisi*, stating the tribunal's considered thoughts on the issue, but at the same time enabling the parties to revisit the issue, if thought appropriate, by applying so to do within, say, a period of 21 days.

30. I repeat that this is a most unusual case in terms of the course which it has taken. I am told by counsel that had the original regulatory decision been that Mr Korner should be the subject of a public reprimand that no appeal would have lain against such a decision, and thus there would have been no necessity for this application.

31. Given this, and given also that this applicant has been forced to ask this tribunal to intercede in the face of an initially severe penalty, a penalty which subsequently was not sought to be defended by the SFC, and wherein serious allegations as to lack of financial integrity have been abandoned, I see no good reason why Mr Korner should not be compensated in costs.

32. Accordingly, in these circumstances I have come to the view that the appropriate and just order as to costs is that Mr Korner is to have the costs of this application for review. I make an order *nisi* to this effect.

Hon Mr Justice Stone
(Chairman)

Mr Marc Harvey of Messrs Linklaters, Solicitors
for the Applicant
Mr Adrian Bell, instructed by the Securities and Futures Commission, for the Respondent