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IN THE INSIDER DEALING TRIBUNAL (3rd DIVISION)
OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION

Founder Holdings Inquiry

In the Matter of an Inquiry into
Certain Dealings in the Listed
Securities of Founder Holdings
Limited

And

In the Matter of an Application to
the Tribunal by CHEUNG Shuen
Lung, Alan, CHEUNG Siu Lung
and Super Highway Ltd

Tribunal: Saunders J, Chairman
 Mr James Wardell, Member,
 Mr Eric Ng Kwok Wai, Member
Date of Hearing: 5 November 2008
Date of Delivery of Ruling: 10 November 2008

Chairman’s Ruling on Questions of Law

Background

1. This is a ruling by the Chairman of the Insider Dealing Tribunal, (3rd Division), made pursuant to paragraph 13 of the Schedule to the Securities (Insider Dealing) Ordinance, Cap 395, (the Ordinance), on certain questions of law. The questions have arisen in the course of the Inquiry into dealings in the listed securities of Founder Holdings Limited, (Founder).

2. By a notice pursuant to s 16(2) of the Ordinance, dated 6 May 2005, (the Notice), addressed to a Chairman of the Insider Dealing Tribunal, the Financial Secretary requested the Insider Dealing Tribunal to conduct an inquiry into certain dealings in the listed securities of Founder. The relevant portion of the Notice reads as follows:

“Whereas it appears to me that insider dealing (as that term is defined in the Ordinance) in relation to the listed securities of a corporation namely Founder Holdings Limited, (“the company”), has taken place or may have taken place, the Insider Dealing Tribunal is hereby required to inquire into and determine:-

(a) whether there has been insider dealing in relation to the company connected with or arising out of the dealings in the listed securities of the company by or on behalf of Julie Kennel on 26 July 2001

(b) in the event of there having been insider dealing as described in paragraph (a) above, the identity of each and every insider dealer;”

3. It is relevant to observe that the Notice identifies “dealings in listed securities” into which inquiry must be made. Whilst asserting the name of the person upon or on whose behalf those dealings are believed to have been undertaken, the Notice does not define or determine who the

persons are, who are “implicated or concerned in the subject matter of the inquiry”. That expression is used in paragraph 16 of the Schedule to the Ordinance. The identification of these persons is important, because only persons falling within that expression are entitled to be present and to take part in the Inquiry and to be represented at the Inquiry by a barrister or solicitor: (Schedule, para 16). Further, it is only such persons, and witnesses, who are entitled to seek costs at an inquiry: (s 26A).

4. Subsequent to the receipt of the s 16 Notice by the Tribunal, the membership of the Tribunal for the Inquiry into Founder was established. Thereafter, the Tribunal appointed counsel to the Tribunal, who, following counsel’s consideration of the available evidence, gave advice to the Tribunal as to the persons considered to be implicated or concerned in the subject matter of the inquiry.

5. Having considered that advice the Tribunal instructed counsel to send “Salmon Letters” to Alan Cheung Shuen Lung, (Alan Cheung), Cheung Sui Lung, (S L Cheung), Super Highway Limited, (Super Highway), Julie Kennel, (Ms Kennel), Peking University Founder Group, (PUF), and Yip Ka Yeung, Albert, (Albert Yip), the Implicated Parties. The Salmon Letters notified each that:

“..the Tribunal has determined that you are a person who is implicated or concerned in the subject matter of the Inquiry and that your conduct in relation to the dealings in the listed securities of the company as described in the notice will be one of the subjects of the Inquiry.”

The Salmon Letter informed each Implicated Party that a preliminary hearing would be held on 28 May 2007.

6. At that preliminary hearing Alan Cheung and S L Cheung were represented by solicitors, Messrs Norton Rose. Super Highway was represented by Ms Liu Chun Ping, (Ms Liu), a shareholder and director of the company, and the sister-in-law of S L Cheung. Ms Kennel, PUF, and Albert Yip did not appear, nor were they represented.

7. At that hearing the Tribunal, in accordance with the procedure recommended by the Salmon Report¹, para 79, publicly stated its terms of reference. At the same time, by way of explanation of its interpretation of its terms of reference and the extent to which the inquiry was likely to be pursued, the Tribunal set out the circumstances leading to the Tribunal taking the view that the extent of the inquiry involved inquiry into dealings by the Implicated Parties.

The application:

8. Now, 17 months after being informed of the terms of reference counsel for Alan Cheung (Mr Harris SC and Ms Lam), S L Cheung and Super Highway (Mr Wong), come to the first day allocated for the substantive hearing of the Inquiry and say that the terms of reference are not sufficiently wide to entitle the Tribunal to inquire into the conduct of their clients.

9. In order to determine this issue the Tribunal must determine whether or not the allegations made against those three parties respectively, in respect of any dealings or other activity coming within the definition of insider dealing, falls within the expression used in the Notice:

¹ Salmon report

“connected with or arising out of the dealings in the listed securities of the company by or on behalf of Julie Kennel on 26 July 2001”.

The important words are “connected with or arising out of”.

10. As I understand the case to be presented, it is, in simple terms this. Mr Alan Cheung, as a director of Founder, had, at least by 16 July 2001, and possibly as early as April 2001, learned of a loss in the accounts of Beijing Founder Order Computer System Co Ltd, (Founder Order), a wholly owned subsidiary of Founder. That loss, which was substantial, was likely to have an adverse impact on the balance sheet of Founder, with a consequent adverse impact on the share price of Founder. It is this information which is contended by counsel to the Tribunal constituted relevant information on the part of Alan Cheung.

11. The case is to be that Alan Cheung was the source of the relevant information by which shares were sold thereby enabling the sellers to avoid a loss. It is argued that the sellers were connected persons by virtue of s 4 of the Ordinance, who obtained their information from Alan Cheung, and that consequently they are liable as insider dealers.

The submissions:

12. The argument by Mr Harris and Mr Wong is straightforward. It is that any activity on the part of the clients they represent cannot properly be shown to be so appropriately related to any dealings by Ms Kennel on 26 July 2001, so as to be able to be said to be “connected with or arising out of” that dealing.

13. If that is the case, they say, then the Tribunal's terms of reference, governed by the terms of the Notice, simply do not encompass any activity on the part of their clients. Consequently their clients should accordingly be released from the Tribunal's Inquiry, and no findings made against them.

The facts relevant to Ms Kennel's dealing on 26 July 2001:

14. Ms Kennel is the sister of Chu Nien Shan, (Ms Chu), who is the wife of Alan Cheung. Although the precise date has not been made available to us, we are informed that Ms Kennel passed away some time between 2007-2008. Throughout the whole of the relevant period she lived in the United States.

15. The case to be presented by counsel to the Tribunal is that Ms Kennel traded in Founder shares through a securities account established at HSBC Broking. The evidence will be that Ms Kennel was accompanied by Ms Chu when Ms Kennel opened her securities account at HSBC Broking. The account began to accumulate Founder shares in Ms Kennel's name from April 2000. By the end of October 2000, 3,844,000 shares were held in the account.

16. No further transactions took place in relation to the shares until 3 May 2001, when 500,000 shares were sold at \$2.15. The remaining 3,344,000 shares were sold on 26 July 2001, (the date in the Notice), at prices ranging from \$1.73 to \$1.77. Ms Chu has asserted to the SFC investigators that the disposal orders for the shares held by Ms Kennel were placed by her on instructions from Ms Kennel.

17. The case is that these transactions were as a result of Ms Kennel or Ms Chu acting upon relevant information supplied by Alan Cheung.

18. Ms Kennel also held an HSBC bank account. According to the account opening documentation, Ms Sandy Ku, (Ms Ku), and Ms Chu were authorised signatories of this account.

19. The proceeds of the sale of Ms Kennel's shares sold on 26 July 2001, \$6,886,909.08, together with the proceeds of the earlier sale of shares on 3 May 2001, a further \$1,075,000, a total of \$7,961,909, remained in Ms Kennel's HSBC Broking account until 5 September 2001. On that day, on the instruction of Ms Chu, the sum of \$7,520,707.34 was withdrawn from the HSBC Broking account and deposited in Ms Kennel's HSBC bank account.

20. On 24 October 2001, Ms Chu withdrew from Ms Kennel's HSBC bank account the sum of \$500,000 in cash, and transferred the sum of \$2 million to Ms Ku's HSBC bank account. On 16 November 2001, Ms Ku, also an authorised signatory on Ms Kennel's HSBC bank account transferred \$5 million to her own HSBC account.

21. The evidence will be that both Alan Cheung and his wife Ms Cheung were the authorised signatories of Ms Ku's bank account, and as I understand that case counsel for the Tribunal will contend that an appropriate inference that arises that Alan Cheung was the ultimate beneficiary of the proceeds of the sale of Ms Kennel's shares in Founder.

The facts in relation to share sales by Super Highway and S L Cheung:

22. Super Highway is a BVI company, the shares of which are owned by S L Cheung's sister-in-law, Ms Liu. She is also the sole director of the company. There appears to be no dispute that, at the relevant time, Super Highway was controlled by S L Cheung.

23. The evidence establishes that prior to 22 May 2001, Super Highway already held Founder Shares. Super Highway acquired a further 686,000 Founder shares between 20 June 2001 and 9 July 2001. Between 22 May 2001 and 21 August 2001, Super Highway sold a total of 10,818,000 shares. As I understand the case it is that the sale of these shares was as a result of the same relevant information, supplied by Alan Cheung, and consequently constituted insider dealing.

24. The allegation is made that S L Cheung traded in Founder shares through a share broking account held by his sister-in-law Ms Liu. The case against S L Cheung is that during the period 15 June 2001 to 7 August 2001, he purchased 280,000 Founder shares and sold 2,190,000 Founder Shares, through Ms Liu's account and that those transactions, being based upon inside information received by S L Cheung from Alan Cheung, constituted insider dealing.

Discussion:

25. It is clear that the extent of the powers of the Tribunal to enquire into insider dealing activity, are limited by the terms of the Notice which contain the terms of reference of the Tribunal: see *Riady v Insider Dealing Tribunal* [2003] 2 HKC 10: see Rogers VP at p 131:

“The notice which institutes that inquiry is required to contain particulars which are sufficient to define the terms of reference of the inquiry.”

It is for the Tribunal to interpret its terms of reference: see *Haughey v Moriarty* [1993] 3 IR 1 (SC). A party dissatisfied with the interpretation of the Tribunal of its terms of reference may challenge that interpretation by way of judicial review.

26. Both Mr Harris and Mr Wong accepted that it was not necessary that the Notice name all potential insider dealers, an expression which encompasses not only those who have bought or sold shares as a result of inside information, but those who supply inside information.

27. Consequently, and I do not understand Mr Harris to dispute this proposition, it is not necessary for the Notice to name Alan Cheung as the source of information leading to the sale by Ms Kennel of her shares on 26 July 2001, for Alan Cheung to be properly before the Tribunal.

28. But as I understand the case for counsel for the Tribunal it is contended that Alan Cheung’s position goes beyond that of a supplier of relevant information enabling the sale by Ms Kennel. It is also contended that he was the source of the relevant information enabling the sale of Founder shares by both Super Highway and S L Cheung.

29. It appears also that counsel for the Tribunal intends to press the matter in relation to the proceeds of sale of Ms Kennel’s shares. A significant point is made of the fact that Alan Cheung was a signatory of Ms Ku’s HSBC bank account, the recipient of \$7 million of the proceeds of sale of Ms Kennel’s shares. I understand that counsel will seek to argue

that Alan Cheung was the ultimate beneficiary of those proceeds.

30. It is quite plain from the foregoing outline of the facts in relation to Ms Kennel's shares, that there can be no argument at all that in the particular circumstances of this case the allegations against Alan Cheung fall within the expression "connected with or arising out of the dealings in the listed securities of the company by or on behalf of the Julie Kennel on 26 July 2001". That must be so if he is the person alleged to have provided the relevant information. It is equally so if it is alleged that he is the true beneficiary of the proceeds of sale.

31. I am satisfied that the terms of reference are sufficiently wide to encompass the activities of Alan Cheung in respect of both the alleged provision of relevant information, and the alleged beneficial advantage of the proceeds of sale of Ms Kennel's shares.

32. The activities of S L Cheung, Super Highway, and Alan Cheung in relation to SL Cheung and Super Highway fall within a quite different category.

33. In the China Apollo Report² the Notice was in the following terms:

"Whether there has been insider dealing in relation to (China Apollo) arising out of the dealings in the listed securities of (China Apollo) by Messrs Lau Chan Wing, Raymond and Zhang Tie Cheng during the period from 1st 10 21st of March 1996 (inclusive)."

² The Report of the Insider Dealing Tribunal of Hong Kong on Whether Insider Dealing Took Place in Relation to the Listed Securities of China Apollo Holdings Ltd between 1 March and 21 March 1996 (Inclusive), dated 6 June 2002.

In considering the extent of the Tribunal's terms of reference arising from the Notice, having noted that the key to the scope of the terms of reference was the phrase "arising out of the dealings in the listed securities of China Apollo", the Tribunal said:

"In other words, the Tribunal looks at what happened in the triangle formed by China Apollo (the named company), Mr Lau and Mr Zhang (the persons named in the notice) and the period of time given in the notice (1 to 21 March 1996), and then establishes facts from the evidence led in relation to those matters, and makes a finding of whether or not insider dealing arose out of that and, if it did, who engaged in that insider dealing. In short, it is by the transactions - the named persons' dealings in the relevant listed securities - that the factual confines of the Inquiry are marked out. By the notice we are authorised and required to look at all facts pertaining to those dealings. Any finding of insider dealing which is supported by these facts is within the ambit of the Inquiry."

34. The analogy of a triangle is, it appears to me, instructive. In the present case, having regard to the terms of the Notice the triangle is formed by Founder, Ms Kennel, and the relevant date, 26 July 2001, all specified both in Notice. Quite plainly, as the primary allegation against Alan Cheung is that he was the provider of the relevant information he, in relation to that transaction, clearly falls within the triangle.

35. The question that requires to be asked is whether S L Cheung and Super Highway can be said to be within that triangle.

36. In my view they plainly cannot.

37. While it may well be that Alan Cheung is also alleged to have provided information in relation to S L Cheung, by which he has traded in Founder shares held by Super Highway, and Founder shares held by Ms Liu, those transactions are plainly quite independent from, and stand alone,

without any connection to the trading of Ms Kennel, other than that Alan Cheung forms a common connecting point to the two triangles.

38. It consequently appears to me plain that the transactions in relation to shares held by Super Highway and Ms Liu are completely unrelated to the transactions stated in the Notice, that of Ms Kennel, other than that Alan Cheung forms a common connecting point to the two other triangles.

39. It is right that Alan Cheung forms a common connection between the three triangles, but in my view it strains the language of the expression “connected with or arising out of” to say that the three groups of dealings fall within that expression. Each is capable of standing alone. The dealings in Founder shares by Super Highway and S L Cheung are not in any way dependent upon any evidence at all in relation to Ms Kennel.

40. It is instructive too, to consider the opening address of counsel to the Tribunal. In outlining the case in relation to the share trading by both Super Highway and S L Cheung no mention whatsoever is made of Ms Kennel. If, as it is necessary to argue having regard to the Notice in its present terms, these transactions arose out of or were connected to Ms Kennel’s dealings on 26 July 2001, one would have expected reference to the connection in the opening address. There is no reference at all.

41. The absence of any reference to any association with Ms Kennel’s transaction reinforces my view that these transactions stand alone, unrelated to, or unconnected with, Ms Kennel’s transactions, save that the same person is alleged to have provided the inside information.

42. There is a second factor, which leads me to conclude that the transactions undertaken by Super Highway and S L Cheung fall outside the context of transactions connected with or arising out of the trading of Ms Kennel on 26 July 2001. That is the identification in the Notice of a specific date, 26 July 2001.

43. The transactions impugned in relation to Super Highway appear to have taken place between 25 May 2001 and 21 August 2001. The transactions impugned in relation to S L Cheung appear to have taken place between 15 June 2001 and 7 August 2001.

44. The evidence establishes two transactions on the part of Ms Kennel. The first, the sale of 500,000 shares was on 3 May 2001. The second, the sale of 3,344,000 shares was on 26 July 2001. The clear inference from the selection of a specific date, and not a range of dates, is that it was the view of the Financial Secretary that the transaction that took place on 3 May 2001, should not be examined by the Tribunal as a possible insider dealing.

45. It is difficult, if not impossible, to see how it can be contended that transactions by Super Highway and S L Cheung over a period ranging from 25 May 2001, to 21 August 2001, can be said to be connected with or arising out of a single day's trading by Ms Kennel on 26 July 2001.

46. For these reasons I am satisfied that the Notice, as it presently stands, confines the Tribunal to examine the transactions undertaken in the name of Ms Kennel on 26 July 2001, to determine whether or not Ms Kennel was an insider dealer, and whether Alan Cheung provided relevant information in relation to those transactions, or whether Alan Cheung was

the ultimate beneficiary of the proceeds of the shares.

47. I am satisfied that the transactions undertaken by Super Highway, and S L Cheung, and the role of Alan Cheung in those transactions are outside the scope of the terms of reference of the Inquiry. Equally, any transactions on the part of PUF and Albert Yip fall outside the terms of reference.

48. I will hear counsel for the Tribunal as to any steps he may wish to take in the light of these findings.

The timing of the application:

49. Mr Harris said in his submission that the Notice, dated 6 May 2005, was “finally provided for the first time to the implicated parties in the core bundle”. He submitted that Alan Cheung, in raising the point, did not seek to delay the Inquiry.

50. The suggestion is entirely disingenuous. Both Alan Cheung and S L Cheung were represented by solicitors 17 months ago, on 28 May 2007, when the Notice was publicly read, and the Tribunal explained its interpretation of the scope of the terms of reference. It is right that Super Highway was represented by its director, Ms Liu, and not solicitors, but on the whole of the circumstances it can barely be said that Super Highway or Ms Liu did not have available to them, if they wanted it, proper advice in relation to the proceedings.

51. The Chairman’s opening statement on that day was transcribed verbatim, and a copy of the transcript supplied to the solicitors

who appeared and Ms Liu. The parties are well aware that the delay, since 28 May 2007, has arisen first because of a number of applications for Judicial Review, and subsequent appeals, in other matters before the Tribunal, which had a potential consequence for this Inquiry, and second because the Tribunal has been engaged in another Inquiry.

52. If any application was to have been made which was not intended to delay the proceedings it ought to have been made many months ago. It is entirely unsatisfactory that these matters should not have been raised until the first day of the substantive hearing.

Late delivery of evidence:

53. Counsel for the Implicated Parties also raised with the Tribunal the fact that it was not until 30 October 2008, that an expert report from Ms Stella Fung was received. The fault in this respect lies with both sides. The correspondence between counsel for the Tribunal and the Implicated Parties' solicitors, soon after the preliminary hearing, make it plain that there were to be delivered eight bundles of evidence. In oversight, only seven bundles were delivered. Those instructing counsel for the Tribunal are at fault for having failed to deliver eight bundles. The solicitors for the Implicated Parties are at fault for having failed to check the number of bundles and make enquiry.

54. The late delivery of the expert report is a matter that can, if necessary, be dealt with by adjournment and the consideration of any incident of costs.

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The availability of the relevant legislation:

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55. On 25 July 2005, in the course of argument on a preliminary point raised in relation to an Inquiry in relation to insider dealing in Asia Orient Holdings Ltd, I raised the question of the availability of the relevant legislation to the public by means of the Bilingual Laws Information System, (BLIS), on the Internet.

56. My concern was that although the Ordinance had been repealed, it remained in force in relation to activity taking place prior to the date of repeal, and consequently ought to have been available on BLIS, with an appropriate note indicating its status. I invited those from the Department of Justice instructing counsel to the Tribunal in that case to take the matter up with the Law Draughtsman so that the issue could be rectified.

57. By 11 August 2005, nothing had been done and I repeated my concern in the Ruling.

58. In the course of this preliminary argument in this Inquiry it was necessary again to check the particular terms of amendment made to the legislation. Three years have gone by now since I raised the matter in order that it may be addressed by the Law Draughtsman in the Department of Justice. When I went to BLIS to check the position this week I found that nothing has been done, and that the links to this legislation remain dead links, merely a statement in relation to each section that the Ordinance has been repealed.

59. This is a thoroughly unsatisfactory situation. Whilst the

Ordinance has been repealed it remains in force in relation to activity occurring prior to its repeal. In those circumstances it ought to be available for any one who might be affected by it to be able to easily access it. It would be a perfectly simple matter to set out the detail of each section of the Ordinance on BLIS, and to endorse a note on each indicating that it has been repealed but remains effective in respect of activity prior to the date of repeal.

60. I would hope that this third request on my part will finally reach the ears of the Law Draughtsman, and this time be listened to.

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

Mr Nicholas Cooney and Mr Jonathan Kwan, counsel to the Tribunal

Mr Jonathan Harris SC and Ms Rachel Lam, instructed by Norton Rose Solicitors, for Mr Cheung Shuen Lung, Alan

Mr William Wong and Mr Harry Liu, instructed by Tsang & Lee Solicitors, for Mr Cheung Siu Lung and Super Highway Limited

No appearance for Ms Julie Kennel

No appearance by or for Peking University Founder Group Corporation

No appearance by or for Mr Yip Ka Yeung, Albert