Application No. 2 of 2003

IN THE SECURITIES AND FUTURES APPEALS TRIBUNAL

IN THE MATTER of a Decision made by the Securities and Futures Commission under section 56(2)(b) of the Securities Ordinance, Cap. 333

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

BETWEEN

WONG PUI HEY, DUNCAN Applicant

and

SECURITIES AND FUTURES COMMISSION ("SFC") Respondent

Tribunal: Hon Mr Justice Stone, Chairman

Roger T Best JP, Member

Professor K C Chan, Member

Date of Hearing: Thursday 25 September 2003

Date of Reasons for Determination: Wednesday 8 October 2003

REASONS FOR DETERMINATION

The Application

1. This is a review of a decision of the Securities and Futures Commission issued on 17 July 2003 against Mr Duncan Wong Pui Hey, pursuant to section 56(2)(b) of the Securities Ordinance, whereby Mr Wong's registration as a dealer was suspended for a period of 6 weeks.

2. By Notice of Appeal dated 6 August 2003 Mr Wong appealed against this decision. More accurately, under the legislation now prevailing this is an application for a review of a decision of which complaint is made: see section 217, Securities and Futures Ordinance, Cap. 571.

3. At the conclusion of the hearing we dismissed this appeal, as it was termed, with costs. We now give our reasons for such dismissal.

Background

4. The applicant, Mr Wong, is licensed with the SFC as a dealer. He joined Victory Enterprises (Investment) Ltd ('Victory') as a dealer's representative in 1996, and from June 1999 onwards he has been registered as a dealing director of Victory.

5. In September 2001 the SFC found that two registered dealer's representatives employed by Victory, a Ms Ho Suk Jan and a Ms Leung Fung Ling, had for a period of 3 years up to June 2001 misappropriated securities held in their client's accounts at Victory. They admitted conducting personal trades in their client accounts, using clients' securities to cover up their own trading losses, and deliberately witholding trading statements from these clients. A total of 79 clients were involved, and the potential loss amounted to some $10.9 million in total, including claims amounting to some $6.1 million in terms of missing stocks. The licences of Ho and Leung were revoked on 15 November 2001 on the basis of serious misconduct involving a fundamental breach of trust.

6. As a consequence of these events, at the request of the SFC Victory appointed a firm of accountants, Messrs HLB

Hodgson Impey Cheng, to investigate the misappropriations and to review the internal control systems of Victory. The report thus prepared identified a number of internal control weaknesses within that firm, which was also found to have exercised little supervision over Ho and Leung.

7. At the material time, the appellant herein, Mr Wong, together with his mother, Madam Lam Wai Ming, were the two dealing directors of Victory, Mr Wong being responsible for daily operations, and for supervising the work of the account executives, including Ho and Leung.

8. During the investigation of the events in this case Mr Wong, as dealing director, attended during 2001 and early 2002 a total of four interviews with the SFC pursuant to section 33 of the Securities and Futures Commission Ordinance, Cap. 24.

9. Consequent upon the information which had been forthcoming during the investigation, the SFC, by letter dated 27 December 2002, wrote to Mr Wong announcing its inquiry under section 56 of the Securities Ordinance into whether he had been guilty of misconduct, and whether he was a fit and proper person to remain registered as a dealer.

10. This letter reviewed the background to the inquiry and detailed the ‘grounds for concern’ arising from that which had occurred in the course of Victory’s operations. In particular, the internal control weaknesses of Victory specified in this letter were lack of supervisory control and segregation of duties, weak control over dealing and settlement procedures, and weak control over distribution of trade documents.

11. In addition to the ‘internal control weaknesses’, a separate category for concern lay in that which was referred to in the letter of 27 December 2002 as the “improper arrangement of ‘private loan’ facilities”. The source of this particular assertion lay in statements made to the SFC by Mr Wong when he was interviewed on 12 September 2001. The substance of that which then was divulged was that at or around the end of 2000 Ho and Leung informed Mr Wong that their clients were unable to settle overdue balances in their accounts, and had requested organization of some sort of financing. As a consequence, Mr Wong had arranged for his brother, Alex Wong, to deposit funds into the bank account of Victory, which then were transferred to the client accounts with the view to reducing the outstanding balances. Mr Wong stated that he had treated these amounts as private loans to clients, and further

had claimed that the sole purpose of such an arrangement was to put pressure upon Ho and Leung to chase their clients to repay the sums due.

12. The SFC took the view that irrespective of the alleged purpose behind such arrangement, this conduct had, directly or indirectly, facilitated the misconduct of Ho and Leung, and that had these defaulting clients (which were all cash clients) been chased for the outstanding balances, the misappropriations of Ho and Leung would have been discovered several months earlier than was the case, and "would therefore have minimized the impact of their misconduct on clients and also on Victory".

13. On the basis of the foregoing, the regulator's 'preliminary conclusion' was that whether Mr Wong was a 'fit and proper person' to remain registered had been called into question, and that it was currently intended to suspend his registration as a dealer, under section 56(2)(b) of the Securities Ordinance, for a 2 month period. Mr Wong accordingly was invited to provide his explanation of the matters in the letter, and to show cause why his registration should not be thus suspended.

14. In response, Mr Wong's solicitors, Messrs Knight & Ho, made detailed representations on behalf of their client in a letter dated 10 February 2003.

15. This letter speaks for itself. The substance of the argument presented was that Mr Wong denied that he had stated that there were any 'private loan' facilities as alleged, and that although it was accepted that Alex Wong indeed had deposited monies into Victory "for the loans to Victory", he had not lent such monies to Ho and Leung, or their clients, as was alleged, that the "sole purpose" of such arrangement had been to put pressure on Ho and Leung in order to press their clients concerned to repay the money owed to Victory, and that the arrangement that had been put in place had never facilitated the fraudulent acts of Ho and Leung.

16. It was acknowledged that "there might be some deficiencies" in terms of internal controls, but that Mr Wong had done his best to ensure Victory's proper operation and had acted honestly at all times, and that in any event "Victory had rectified all deficiencies."

17. By letter of 17 July 2003 the SFC stated that it had carefully considered the representations made, and enclosed a

notice of their decision, under section 56(2)(b) of the Securities Ordinance, to suspend Mr Wong's registration for a period of 6 weeks.

18. The Statement of Reasons for this decision, issued under section 57(4) of the Ordinance, carefully and in detail rehearsed the representations made on behalf of Mr Wong in correspondence and, at paragraphs 10-12 thereof, set out the response to these representations.

19. As to the internal control weaknesses, the conclusion drawn was that Victory's system was sufficiently poor so that Ho and Leung were able to perpetrate their fraudulent activities for some 3 years affecting the interests of about 79 clients, and that there was no dispute that Mr Wong was responsible for the daily operations of Victory's business. Accordingly, the deficiencies identified were "directly attributable" to Mr Wong and to his failure to discharge his function of properly managing and supervising the business.

20. As to the denial of private loan facilities, the SFC took the view that the explanation of the whole arrangement was "totally implausible", and that the documentary material previously

provided by Mr Wong on 22 March 2002 demonstrated that sums deposited by Alex Wong were used to reduce outstanding balances in certain client accounts, and that when money had been collected from these clients, this would be used to settle the buy transactions of Alex Wong. Accordingly, it was concluded that the arrangement was a loan arrangement, notwithstanding the lack of any documentation, and that had the clients of Ho and Leung been contacted directly about repayment of the outstanding balances, the latters' defalcations would have been earlier discovered.

21. The result, therefore, was that the initial findings of the SFC were confirmed. In terms of penalty, however, consideration was accorded to all the mitigating factors, and it was accepted that Mr Wong had reported the matter to the SFC, that he had co-operated fully during the investigation, and that all client losses had been compensated promptly. Accordingly, the 2 month suspension originally mooted was reduced to a 6 week suspension of Mr Wong's dealer registration, although it was considered that the supervisory failures "were so pronounced and continued for such a long period of time, facilitating client losses, that a suspension is required."

22. Mr Wong is aggrieved by this decision. Hence this application.

Submissions

23. On behalf of Mr Wong, Mr Simon Chan adopted that which basically was the two-pronged approach earlier rehearsed in correspondence between the SFC and Messrs Knight & Ho.

24. At the outset, Mr Chan agreed and accepted that there had been "some deficiency" in terms of the internal control procedures within Victory, but nevertheless he submitted that the penalty of a 6 week suspension had been too severe, and that the appropriate penalty should be no more than a reprimand, and preferably a private reprimand (Victory having been publicly reprimanded by the SFC in July 2003 consequent upon these events).

25. Mr Chan's other main submission, and one upon which he was pressed by the tribunal, was that as a matter of fact and law the SFC had been wrong to conclude that this was a situation in which there had been 'loans' to private clients of Ho and Leung which had been arranged by Mr Wong, as alleged or at all. He further argued that there was no causal linkage between the misconduct of

Ho and Leung and the 'financial arrangement' that had been put into place, and he disputed that this arrangement had had any effect in facilitating the defalcations of Ho and Leung.

26. For the SFC, Miss Pak strongly submitted that the previous reported SFC cases relied upon by Mr Chan wherein the penalty had been confined to a public reprimand were clearly distinguishable on the basis that these latter instances had *solely* represented instances of failure of supervision.

27. However the present case, she said, contained that which she termed an additional, and highly significant, "approbation factor", in that the applicant had acted improperly in putting into place the financial arrangements that he did, and that notwithstanding argument as to the characterization of these arrangements, the essence of the SFC position, and the justifying factor underpinning the disciplinary decision taken in this case, was that in the view of the SFC such financial arrangement had, directly or indirectly, served to facilitate the misconduct of Ho and Leung.

28. This had occurred, Miss Pak argued, by reason of the fact that the infusion of funds by Alex Wong had produced a distorted

picture in the monthly statements sent to clients (wherein the statements sent to clients would show merely the set-off date of the sale and purchase transactions as the settlement date of the amount outstanding, as opposed to any date of actual repayment) and also served to obscure the fact of misappropriation of stocks, since the money provided by Alex Wong resulted in a situation in which Victory thus did not pursue these clients directly for repayment of sums outstanding, but was content to rely upon Ho and Leung to do so – when the latter, of course, were in the process of misappropriating the stocks in order to cover their own trading losses.

29. Miss Pak further submitted that not only did the circumstances of this arrangement make no commercial sense, but in the view of the SFC had this financial arrangement not been in operation, the incidents of misappropriation would have been exposed earlier than in fact was the case, and hence the losses suffered by Victory and its clients significantly reduced.

Determination

30. In our view it is difficult to discern any merit in this review application. We agree with the submissions on behalf of

the SFC, made both orally and in the extensive skeleton argument filed on its behalf.

31. The precise characterization of the entirely curious financial arrangements which were put into place seems to us not to be of great significance, given that on the information available the SFC clearly were justified in finding that monies deposited by Alex Wong in fact *were* credited to certain client accounts: see in particular here the explanatory letter dated 15 February 2002 signed by the applicant herein, Mr Wong, and sent to the SFC, which detailed the crediting of various sums in May, June and July 2000 to specified client accounts, as is exemplified by the accompanying ledger extract.

32. Similar information, and a fuller statement of the position, appears in the translation of the signed statement of Mr Wong made to the SFC on 22 March 2002 [Exhibit WPH-13] which includes a statement by Mr Wong (at paragraph 5 thereof) that in terms of the outstanding balances on Ho's client accounts he would tell Ho that he had arranged a "temporary loan" for her clients and ask her to press her clients to settle the outstanding balance as soon as possible.

33. We appreciate that Mr Wong now wishes to disavow any suggestion that the arrangement that was in place properly could be construed as a 'loan', and we note that in his skeleton argument at least (albeit not in oral submission) Mr Chan had suggested that Mr Wong had not fully appreciated the legal significance of the content of his statement of 22 March 2002. This, no doubt, was the precursor to Mr Chan's submission that there was never any debtor/creditor relationship between the clients of Ho and Leung and Alex Wong, and thus that the SFC was purporting to punish for something that, legally and factually, had not occurred.

34. We do not consider that this submission has any force. The stark reality of the situation is that monies came into Victory's account, and in turn variously were credited to certain client accounts. On the information available we fail to see how this primary fact can be gainsaid, despite Mr Chan's efforts to do so. His client had made this position abundantly clear both in correspondence and in statement form; as he put it in his statement to the SFC (at paragraph 4): "we came up with an arrangement in which A Wong would deposit money into the company account to settle the outstanding balance of the accounts of Miss Ho's clients temporarily".

35. Accordingly, given the undoubted infusion of money and the crediting of such sums as plainly occurred, whilst the clients in question may have been unaware of what was going on in their accounts (which is unsurprising given the clear misconduct of Ho and Leung, and the misappropriation of scrip that was but subsequently revealed), and whilst arguably there may have arisen no contractual nexus between Alex Wong and these clients, at the end of the day we are unable to accept that these are matters of any real significance.

36. Whilst the use by the SFC in the Statement of Reasons of the words "private loans to certain client accounts of Ho and Leung" appears to have paved the way for that which we regard as narrow (and ultimately unmeritorious) legal argument, the factual underpinning giving rise to this description is unchanged; had the wording used alternatively referred, for example, simply to 'acting improperly by putting in place financial arrangements whereby certain client accounts of Ho and Leung were artificially credited', or some such other description to represent that which undoubtedly took place, the factual matrix the subject of the present complaint would have remained precisely the same, albeit the scope for argument diminished. In so saying, we make no criticism of the manner in which the Statement of Reasons was couched, not least

because the term ‘loan’ was that used by Mr Wong in his fourth SFC statement, understandably in that monies indeed were notionally ‘loaned’, in the general sense at least, to the accounts in question.

37. So in our view there is nothing of substance in Mr Chan’s submissions on the ‘loans’ point. In light of the available evidence before the SFC in terms of that which transpired in and with the operation of these accounts, it seems to us that the SFC were justified in adopting the stance that they have in this case.

38. It remains only to add that we remain sceptical, to say the least, about the apparent rationale for the ‘financial arrangements’ (to use the neutral term) that were put in place by Mr Wong. We pressed Mr Chan on this. We find it difficult to accept at face value the true reason for that which Mr Wong says that he did, although we agree with the contention that that which actually was done served to obfuscate and disguise the true financial situation pertaining to these client accounts.

39. In this connection we agree with Miss Pak that there was no logical reason why the arrangements as were put in place could be thought to exert pressure on Ho and Leung, or their clients, to

make prompt repayment; to the contrary it seems to us that, far from creating a sense of urgency in terms of monetary recovery, Ho and Leung would have regarded such recovery of outstanding balances as less pressing, given the appearance thus created that such balances temporarily had been settled by the infusion of money from Alex Wong. We comment, further, that the characterization as "totally implausible" of the avowed reason for that which occurred if anything understated the position.

40. The foregoing observations dispense with the first two grounds within Mr Chan's Notice of Appeal. The third and final ground of appeal is that a suspension of 6 weeks in the circumstances of this case is and was "manifestly excessive". This ground details the mitigating factors in terms, for example, of that which was done by Mr Wong to rectify the situation and in terms of his co-operation with the regulator, which it is said that the SFC "failed to consider or consider sufficiently" in the circumstances of this case.

41. We were unable to agree with this submission either. It is clear to us that in assessing the penalty the SFC took all relevant matters into account and reached its decision in light of all the facts.

42. An appellate/reviewing tribunal is in principle reluctant to interfere with a decision handed down by a regulator statutorily charged with overseeing the operation of a particular market *unless* it can be demonstrated that a clear error has been made, for example, in terms of a failure to take relevant matters into consideration, or conversely, that matters which have been taken into account ought not to have been placed within the discretionary 'mix'. Each case obviously will depend upon its own particular facts, but it should not be thought that a tribunal of this nature readily will accept invitations to interfere with the exercise of the discretion of the regulator in the field and to substitute its own judgment or assessment of the position unless it can be demonstrated that good and cogent reason exists for so doing.

43. In our view, nothing that has been said in this review has succeeded in persuading us that there should be any interference with the SFC decision in the circumstances of this particular case.

44. We thus dismissed this application for review and confirmed the decision of the SFC as contained in its Notice of Decision dated 17 July 2003.

45. As to costs, we were and are able to see no basis for a conclusion other than that costs of this review should follow the event, and that such costs should be paid by the unsuccessful applicant to the SFC. Section 223 of the Securities and Futures Ordinance, Cap. 571 provides that the tribunal may award "such sum as it considers appropriate" in respect of costs reasonably incurred by a party in relation to the application for review and of the review itself, and in this connection we anticipate that a summary of such costs as are sought to be recovered in this case will be submitted to the tribunal for decision thereon.

46. In light of the fact that our reasons for determination were not given contemporaneously with our announcement of dismissal of this application at the conclusion of argument, the tribunal will further entertain the unsuccessful applicant if and in so far as he wishes to make any representation in terms of costs.

Hon Mr Justice Stone (Chairman)	Roger T Best (Member)	Prof K C Chan (Member)

Mr Simon Chan, instructed by Messrs Knight & Ho, for the Applicant

Miss Doris Pak, of the Securities and Futures Commission, for the Respondent