

SFC obtains court order to disqualify former chairman of Pearl Oriental Oil Limited for six years

25 Jan 2018

The Securities and Futures Commission (SFC) has obtained an order in the High Court to disqualify Mr Fan Di, former chairman, president and executive director of Pearl Oriental Oil Ltd (Pearl Oriental) for defalcation, misfeasance and other misconduct towards the company (Note 1).

The Honourable Mr Justice Godfrey Lam granted the order to disqualify Fan from being a director or being concerned or involved in the management of any listed or unlisted company in Hong Kong including Pearl Oriental or any of its subsidiaries and affiliates, without the leave of the court, for six years (Notes 2, 3 & 4).

The SFC's investigation found that from April 2003 to June 2005, Fan caused Pearl Oriental to invest RMB60 million via an investment company on the Mainland, which would lend the money to companies connected to Fan. In July 2005, Pearl Oriental's auditor queried the recoverability of the investment, which was itself objectionable because no written approval had been obtained from the board of Pearl Oriental. Upon demand from Pearl Oriental in August 2005, RMB 64.8 million (purportedly as principal plus interest) was repaid to Pearl Oriental.

Immediately upon the repayment, Fan caused Pearl Oriental to pay out RMB64.5 million, again without the board's approval, as an advance for an acquisition of a Mainland logistics business. In obtaining retrospective board approval for the acquisition, Fan failed to disclose important unfavourable findings emerged in the due diligence on the logistic business and to present accurate information about its valuation. As a result, the board approved the payment without taking any reasonable steps to verify the information presented by Fan.

However, the RMB64.5 million was actually transferred to Mainland companies connected to Fan. The acquisition of the logistics business did not proceed in the end and Pearl Oriental incurred a substantial loss of the RMB64.5 million (Note 5).

End

Notes:

1. The company was known as China Merchants DiChain (Asia) Limited at the material times and as Pearl Oriental Innovation Limited at the time the SFC commenced the proceedings. It was listed on the Main Board of the Stock Exchange of Hong Kong Limited in April 1993. The company was principally engaged in provision of logistics services on the Mainland at the material times.
2. Under section 214 of the Securities and Futures Ordinance, the court may make orders disqualifying a person from being a company director or being involved, directly or indirectly, in the management of any corporation for up to 15 years, if the person is found to be wholly or partly responsible for the company's affairs having been conducted in a manner involving defalcation, fraud or other misconduct.
3. The SFC has obtained disqualification orders against the three other directors in these proceedings under section 214 of the SFO. Please see the SFC's press release dated [24 May 2011](#).
4. **When the investigation commenced in 2007, Fan had left Hong Kong and could not be located to effect service of the proceedings until September 2013. On 26 June 2017, the SFC and Fan agreed to dispose the proceedings by Carecraft procedure which involves the submission by both parties to the court of an agreed statement of facts upon which the court will assess what order should be made.**
5. In 2007, Pearl Oriental obtained judgment against Fan (and other related parties including two other former executive directors of Pearl Oriental) for the sum of RMB64.5 million.
6. A [summary](#) of the material events and the allegations are posted on the SFC's website (www.sfc.hk). **Fan is the "Other Director" referred therein.**

Summary of the Facts

(an extract from the SFC's Petition filed with the Court)

A. Transactions entered into by Pearl Oriental Innovation Limited (“the Company”) and its subsidiaries during the period from 2003 to 2005 (“Relevant Period”)

1. DiChain Holdings Limited (“DC Holdings”) is a limited company incorporated in Hong Kong. It was at all material times the ultimate holding entity of the Company beneficially interested in 2,500,000,000 (55.11%), 2,500,000,000 (55.11%) and 3,032,698,894 of the Company’s issued shares as at 31 March 2003, 31 March 2004 and 31 March 2005 respectively.
2. Li Xinggui (“Mr. Li”) and Zheng Yingsheng (“Mr. Zheng”) were directors of the Company from 26 August 2002 to 31 December 2005 and from 27 March 2003 to 1 September 2010 respectively. Zhou Li Yang (“Mr. Zhou”) has been a director of the Company since 17 September 2004. Mr. Li, Mr. Zhou, Mr. Zheng and another director of the Company at the Relevant Period (“the Other Director”) are collectively referred as “the Directors”.
3. DiChain Warehouse Services (Shenzhen) Co., Ltd (迪辰倉儲服務(深圳)有限公司) (“DC Warehouse”) is a wholly foreign owned enterprise in the PRC. It was at all material times an indirect wholly owned subsidiary of the Company.
4. During the Relevant Period, the Directors or some of them, have caused:-
 - 4.1 DC Warehouse to invest RMB60,000,000 through Shenzhen International Trust and Investment Co. Ltd. (深圳國際信託投資有限責任公司) (“SZITIC”) (Section B); and
 - 4.2 the Company and/or DC Warehouse to pay RMB64,500,000 to Hero Vantage Limited (“Hero Vantage”) for the purported acquisition of Yixing

Wangda Logistics Co. Ltd. (宜興市旺達物流有限公司) (“Wangda”) in the PRC (Section C),

in circumstances where their conduct involved misfeasance or misconduct towards the Company, its members or part of its members, or resulted in its members or part of its members not having been given all the information with respect to its business or affairs that they might reasonably expect.

B. RMB60,000,00 investment through SZITIC

5. Between 21 April 2003 and 20 June 2005, DC Warehouse entered into 12 agreements (“Trust Fund Agreements”) with SZITIC, pursuant to which:-
 - 5.1 DC Warehouse paid a total of RMB60,000,000 to SZITIC qua trustee; and
 - 5.2 SZITIC would lend the RMB60,000,000 to third parties to earn interest.
6. The Other Director alone made the decision to invest the RMB60,000,000 via SZITIC. In doing so, he had not obtained or attempted to obtain any prior approval from the board of directors or shareholders of DC Warehouse.
7. On 25 July 2005, the Audit Committee of the Company held a meeting which was attended by Mr Zhou, the then company secretary and financial controller, accountants of Deloitte Touche Tohmatsu (“Deloitte”) (which was then the auditors of the Company) and two independent non-executive directors. During that meeting, the independent non-executive directors complained that the Audit Committee was only informed of the investment via SZITIC after it had been made. The accountants also expressed their concern over the recoverability of the RMB60,000,000 invested and demanded that the Company should either call back the investment or obtain a list of borrowers from SZITIC so that Deloitte could review and assess their credibility.

8. After the Audit Committee meeting, the then company secretary and financial controller tried but failed to obtain from SZITIC a list of the borrowers to which the RMB60,000,000 had been lent. In the light of this, it was decided that DC Warehouse should call back the investment from SZITIC.
9. Between 3 August 2005 and 9 August 2005, SZITIC repaid to DC Warehouse the invested sums with interest, amounting to a total of RMB64,840,849.99. On 10 August 2005, SZITIC issued a certificate confirming the termination of the Trust Fund Agreements and the repayment of all sums invested with interest. This was the only written confirmation from SZITIC obtained by the then company secretary and financial controller and Deloitte at that time.
10. In the course of its investigations, the SFC has obtained the following information which was never revealed to the then company secretary and financial controller or Deloitte at the material time:-
 - 10.1 One characteristic of the RMB60,000,000 investment via SZITIC was that DC Warehouse would designate the third parties to which SZITIC would lend the sum.
 - 10.2 Upon the instructions from DC Warehouse, SZITIC had lent RMB45,000,000 to Company A and RM15,000,000 to Company B. Both Company A and Company B are incorporated in the PRC. The Other Director was at all material times the legal representative, Chairman and General Manager of both of these companies.
11. As stated in Section C below, although between 3 August 2005 and 9 August 2005 DC Warehouse received RMB64,840,849.99 from SZITIC, during the same period DC Warehouse paid RMB64,5000,000 to another PRC company ("Company C"), a company related to the Other Director (see paragraph 21 below), through which RMB57,005,000 went back to Company A and Company B again in the period from 3 August to 19 October 2005. RMB55,840,849.99 out of the RMB57,005,000 was immediately re-directed back to SZITIC.

C. Purported acquisition of Wangda

12. Wangda operated logistics business in Yixing (宜興市) in the PRC. It was owned by 宜興市交通資產管理有限公司 (70%) and 宜興市宜港裝卸儲運有限公司 (30%) until about November 2006 when it became wholly owned by the former. Its legal representative and general manager at all material times was Mr Kong Baisong 孔柏松 (“Mr Kong”).
13. DC Holdings had in the past operated a beer factory in Yixing. When the Yixing government later resumed the land on which the factory was built, it had then granted to DC Holdings a separate piece of land also in Yixing. Instead of continuing with its beer production business, DC Holdings proposed to operate logistics business on that new piece of land, but the Yixing government rejected that proposal. The Other Director, Mr Li and Mr Li Haozhang 李浩璋 (Vice President of DC Holdings at the time) thereafter had looked for another site for similar purpose and the Yixing government enquired with DC Holdings if it would be interested in working with Wangda.
14. On or about 13 December 2004, Mr Zhu Runlin 朱潤林 (“Mr Zhu”) prepared a report on the logistics business of Wangda and addressed the same to the Other Director, Mr Wu Shiyue 伍世岳 (“Mr Wu”) (an executive director of the Company from 2002 to 30 August 2005) and Mr Li Haozhang 李浩璋 (Vice President of DC Holdings at the time) or Mr Li Xinggui. Mr Zhu had been employed the Other Director to explore investment opportunity in the PRC on behalf of DC Holdings and the Company. It was stated in Mr Zhu’s report that:-
 - 14.1 a number of parties were interested in investing in Wangda and were actively negotiating for investment opportunities;
 - 14.2 the Yixing government was inclined to cooperate with a Hong Kong company called Hero Vantage Limited (“Hero Vantage”), which had business in the PRC;

- 14.3 the director and majority shareholder of Hero Vantage was Mr Li Shenan 李深恩, who had an edge in the negotiations because of his connections in Yixing;
- 14.4 however, Mr Li Shenan did not have sufficient funds and intended to bring in a strategic shareholder for finance;
- 14.5 Mr Zhu had already explored the possibilities of cooperation with Mr Li Shenan and the latter's feedback was positive; and
- 14.6 the management was advised to carry out further investigations into the Wangda acquisition.
15. On 7 July 2005, the Company and DC Holdings held a joint board meeting, which was attended by the Other Director, Mr Wu, Mr Li, Mr Li Haozhang and others (but not Mr Zheng and Mr Zhou). In that meeting, Mr Li Haozhang and Mr Zhu reported that:-
- 15.1 Hero Vantage and Wangda had reached a consensus that the former would acquire Wangda's logistics assets including its land;
- 15.2 DC Holdings had discussed with Hero Vantage and it was recommended that the Company or DC Holdings would acquire 70% of the shares in Hero Vantage so as to obtain control of Wangda's logistics assets;
- 15.3 the estimated value of Wangda's logistics assets was HK\$180 million; and
- 15.4 Mr Li Shenan had agreed to sell 70% of the shares in Hero Vantage to the Company or DC Holdings for HK\$60 million, which he would then use to acquire Wangda's logistics assets.
16. It was unanimously resolved in that joint board meeting on 7 July 2005 that:-

16.1 the Company would be the corporate vehicle to cooperate with Hero Vantage or acquire the latter's shares;

16.2 given that the Company was a listed company and the board of directors of the Company would need time to consider and approve the Wangda acquisition, DC Holdings would first enter into relevant agreements with Hero Vantage;

16.3 should the Company later approve the acquisition, it would then enter into formal agreements with Hero Vantage, after which DC Holdings would drop out; otherwise, or should the matter remain unresolved within three months from the joint board meeting, DC Holdings would proceed with the acquisition in accordance with the agreements it had signed with Hero Vantage; and

16.4 given the transitory role of DC Holdings, an internal fund transfer from, or loan by, the Company to it would be desirable and should the Company decide subsequently not to proceed with the acquisition within the next three months, DC Holdings would repay the same amount to the Company.

17. In this regard, the SFC has tried but failed to obtain any evidence of:-

17.1 any transitory agreement entered into by DC Holdings and Hero Vantage pending the consideration and approval by the board of directors of the Company of the Wangda acquisition; or

17.2 any internal fund transfer or loan as between the Company and DC Holdings,

albeit both had been resolved in the joint board meeting.

18. On or about 21 July 2005, Hero Vantage issued a payment notice to both the Company and DC Holdings, which were thereby requested to make payments to

Company C in the amount stated in two agreements, namely, 《資產轉讓預付款協議》 (“July 2005 HV Deposit Agreement”) and 《借款協議》 (“July 2005 HV Loan Agreement”), both of which were allegedly entered into on 19 July 2005.

19. The SFC cannot locate the July 2005 HV Deposit Agreement and the July 2005 HV Loan Agreement. However, the SFC has obtained two other agreements entered into by Hero Vantage and the Company (with the Other Director signing on its behalf) dated 27 September 2005. These two agreements are also named 《資產轉讓預付款協議》 and 《借款協議》 and to avoid confusion they are referred to as “September 2005 HV Deposit Agreement” and “September 2005 HV Loan Agreement” respectively.

19.1 Under the September 2005 HV Deposit Agreement, the Company agreed to pay Hero Vantage a deposit of HK\$42,000,000 for the purpose of the acquisition of certain logistics business assets in Yixing.

19.2 Under the September 2005 HV Loan Agreement, the Company agreed to lend Hero Vantage HK\$18,000,000 for a period of 2 years with interest at 4% per annum.

20. DC Warehouse, presumably in compliance with the payment notice referred to in paragraph 18 above, transferred a total of RMB64,500,000 (RMB equivalent of HK\$60,000,000) to Company C within seven days from 3 August 2005 to 10 August 2005. Remarkably, such payments had been made contemporaneously with the repayment of RMB55,840,849.99 by Company A and Company B to SZITIC and the refund of RMB64,840,849.99 by SZITIC to the Company between 3 August 2005 and 9 August 2005.
21. At the time of such payment by DC Warehouse, the legal representative of Company C was a PRC citizen, who owned 90% of the shares in Company C and was one of its directors. He was also a relative of the Other Director.

22. From 3 August 2005 to 19 October 2005, Company C transferred RMB68,617,499.32 to different PRC companies which did not have or appear to have any involvement in the Wangda acquisition, or in any way associated with Hero Vantage. Company A and Company B were two of the transferees receiving RMB41,855,000 and RMB15,150,000 respectively.
23. The result of this round-robin cash flow was that RMB55,840,849.99 out of the RMB64,840,849.99 repaid by SZITIC was immediately re-directed via Company C to Company A and Company B and then back to SZITIC for no discernable commercial reasons.
24. On or about 15 August 2005 the Other Director instructed Mr Chong Siu Po 莊少波 (“Mr Chong”), an assistant vice president of the Company, and Mr Liu Jun 劉軍 (“Mr Liu”), the chief accountant of DC Holdings, to carry out a due diligence exercise of Wangda in Yixing.
25. Mr Chong and Mr Liu carried out the due diligence exercise of Wangda from 18 August 2005 to 20 August 2005. They prepared a due diligence report and submitted the same to the Other Director and Mr Li Haozhang only. In the report, Mr Chong and Mr Liu identified various problems with the business of Wangda and their assessment of the merit of the proposed acquisition was unequivocally not favourable.
26. On 5 September 2005, a meeting was held with the Yixing government officials and Mr Kong, with Mr Li Haozhang and Mr Liu attending on behalf of DC Holdings. The following matters had been discussed in the meeting in relation to the Wangda acquisition:-
 - 26.1 DC Holdings would set up a new company in Yixing for the purposes of acquiring Wangda’s logistics assets;
 - 26.2 the acquisition price would be determined by a third party, to be appointed by DC Holdings and Wangda;

26.3 the actual usable area of land to be acquired would take into account the land held by DC Holdings in Yixing (i.e. the land granted by the Yixing government referred to in paragraph 13 above); and

26.4 DC Holdings would not be taking over the liabilities of Wangda.

27. Up to 5 September 2005, all the discussions amongst the Yixing government, Wangda and DC Holdings or the Company were preliminary and the parties had never agreed on anything concrete capable of being implemented. In particular, what had been proposed by DC Holdings to Wangda and the Yixing government was that:-

27.1 it would acquire all the tangible assets of Wangda, but not its land and liabilities;

27.2 it would not acquire the shares of Wangda and hence after the acquisition would not be using those tangible assets in the name of Wangda; and

27.3 it would exchange the piece of land previously granted by the Yixing government to DC Holdings for the land occupied by Wangda, so the acquisition would not include the land of Wangda.

28. In or about September 2005, Mr Kong and Mr Liu on behalf of Wangda and DC Holdings respectively engaged an accountants firm in Wuxi called 無錫普信會計師事務所有限公司 (“Wuxi Accountants”) to value Wangda’s logistics fixed assets. The Wuxi Accountants later produced a draft report valuing Wangda’s fixed assets at RM56,447,433.40 as at 31 August 2005, without taking into account the value of Wangda’s land in Yixing and its debts. Mr Liu considered the valuation excessive and refused to accept it as the basis for further negotiations.

29. On 26 September 2005, the Other Director, Mr Li, Mr Zheng and Mr Zhou attended a board meeting of the Company. Another valuation report prepared by Shenzhen Guosong Assets Appraisal Co. Ltd. 深圳市國頌資產評估有限公司 (“Guosong Report”) dated 22 September 2005 and an Assets Acquisition Proposal for Wangda were tabled in that meeting. As shown in the Guosong Report:-

29.1 Shenzhen Guosong Assets Appraisal Co. Ltd. had been instructed to value the assets of Wangda including its land; and

29.2 Wangda’s logistics assets were valued at RMB185,752,400.

30. The Other Director , who was then the only director in the Company involved in the negotiations in the proposed acquisition of Wangda, reported in the meeting that:-

30.1 the Yixing government was restructuring the operations of Wangda, and Hero Vantage, being an independent third party not connected to either the Yixing government or the Company or any of its directors under the Listing Rules, had agreed to acquire all the logistics assets from Wangda;

30.2 the Company was considering the option of acquiring Wangda’s logistics assets through the acquisition of controlling equity interest in Hero Vantage;

30.3 he had been informed by officials of the Ministry of Communications 國家交通部 that the Yixing government would subsidise any company operating logistics business in the Yangtze Delta region, and the logistics business in Yixing might be able to obtain RMB20,000,000 to RMB30,000,000 in subsidy;

30.4 there were other parties interested in acquiring Wangda’s logistics assets, so that it was urgent for the Company to put up a deposit for the acquisition; and

30.5 DC Holdings had already paid over RMB60,000,000 on behalf of the Company as deposit for the Wangda acquisition, and he wanted the approval from the board so that the Company could reimburse DC Holdings for that RMB60,000,000 and proceed with the acquisition.

31. However, the Other Director had not revealed to other members of the board at the meeting on 26 September 2005 of:-

31.1 the due diligence report prepared by Mr Chong and Mr Liu;

31.2 the draft report by the Wuxi Accountants; or

31.3 the fact that the Wangda acquisition would not (or at least might not) include its land or liabilities.

32. Under such circumstances, the board of directors of the Company unanimously approved on 26 September 2005 all the previous prepayments to Company C, in order to secure obtaining the interests in the Wangda acquisition and the acquisition of controlling equity interests in Hero Vantage.

33. The proposed acquisition of Wangda had never proceeded to completion. In or about June 2006, the Stock Exchange received complaints alleging that the Other Director, Mr Zhou and Mr Li Haozhang had misappropriated funds of the Company and referred the same to the management of the Company. A special unit was set up by the board of directors of the Company to investigate the matter. When being questioned by the special unit, the Other Director explained that the proposed acquisition of Wangda had fallen through because:-

33.1 it was discovered in subsequent investigations that Wangda had in fact incurred debts of over RMB200,000,000;

33.2 Hero Vantage requested that the proposed acquisition of Wangda would exclude the latter's debts but such request was rejected by the Yixing government; and

33.3 as a result, the negotiations came to a standstill and failed in the end.

34. Such explanation is false and untrue.

PARTICULARS

34.1 The negotiations for the Wangda acquisition in fact came to a halt much earlier after the Wuxi Accountants finished the draft valuation report because Mr Liu was not satisfied with the results.

34.2 The parties had no discussion thereafter and in December 2005, the Yixing government and Wangda concluded that the project had failed.

34.3 Wangda had never incurred debts of over RMB200,000,000.

34.4 Hero Vantage and Company C had never been involved in the negotiations for the Wangda acquisition.

34.5 Wangda had never received payment from the Company or DC Holdings or any of their connected companies.

D. Liability of Mr Li, Mr Zheng and Mr Zhou

35. The payment of RMB64,500,000 via DC Warehouse to Company C were disclosable transactions under the Listing Rules. However, Mr Li, Mr Zheng and Mr Zhou had failed to take any steps to procure the Company to make the necessary announcements and notification as required under Rules 13.13, 13.20, 14.34 and 14.38 of the Listing Rules.

36. By virtue of the Declaration and Undertaking given and signed by Mr Li, Mr Zheng and Mr Zhou under the Listing Rules, they have undertaken to comply to the best of their abilities with the Listing Rules from time to time in force.
37. Given that Mr Li, Mr Zheng and Mr Zhou are also obliged by Rule 3.12 of the Listing Rules to accept and have at all material times accepted full responsibility, collectively and individually, for the Company's compliance with the Listing Rules, they must be responsible for the non-compliance pleaded above.
38. Further, in causing the Company to make the said payment and yet failing to procure proper compliance with the Listing Rules, Mr Li, Mr Zheng and Mr Zhou have acted in breach of their duties under Rule 3.08(c) and 3.08(f) of the Listing Rules.
39. In the premises, Mr Li, Mr Zheng and Mr Zhou have conducted the business or affairs of the Company in a manner resulting in its members or part of its members (other than themselves) not having been given all the information with respect to its business or affairs that they might reasonably expect.

E. Civil Action and Stock Exchange's Disciplinary Action

40. On 31 August 2006, the Company commenced civil proceedings in HCA No. 1893 of 2006 against DC Holdings, Mr Li and other parties involved to recover the loss of RMB64,500,000 in the proposed Wangda acquisition. Judgment in default of defence was obtained against Mr Li and some of the parties on 16 October 2007.
41. On 30 April 2008, the Listing Division of the Stock Exchange commenced disciplinary proceedings against the Company. On 7 January 2009, the Listing Committee conducted a hearing and concluded that the Company has acted in breach of Rules 13.13, 13.20, 14.34 and 14.38 of the Listing Rules. No appeal has been lodged against the decision of the Listing Committee.