



## Court Orders Sound Global Chairman to Purchase Investors' Shares

The Securities and Futures Commission (the **SFC**) has obtained an order in the Court of First Instance for the chairman and executive director of Sound Global Limited (**Sound Global**), Mr Wen Yibo (**Wen**), to purchase shares held by the other shareholders of Sound Global at a price to be determined by the court. The order was made against Wen under Section 214 of the Securities and Futures Ordinance (the **SFO**) for having orchestrated schemes to falsify the bank balances of Sound Global and its three wholly owned subsidiaries (the **Group**) and fabricate relevant bank statements and balance confirmations. This resulted in the bank balances of the Group stated in its audited financial statements for 2012 and 2013 being inflated by RMB 2.18 billion and RMB 2.72 billion, respectively, representing 82% and 89% of the Group's reported net assets. This was the first time a share purchase order has been made under Section 214 of the SFO.

The court also issued a 12-year disqualification order against Wen and ordered him to pay the costs incurred by Sound Global and the SFC.

The [judgment](#) is available on the judiciary's website (Court Reference: HCMP868/2019).

### Factual Background

Sound Global is an investment holding company that was listed on the Main Board of the Hong Kong Stock Exchange from 30 September 2010 until its shares were suspended from trading on the 13 April 2016. It was also listed on the Singapore Exchange Securities Trading Limited from 6 October 2006 until 27 January 2014 when it was voluntarily delisted.

In 2015, an equities research firm issued two reports on Sound Global suggesting that the Group's actual cash and bank balances amounted to only one third of the amounts reported in its 2013 audited financial statements and that its actual profits were only a quarter of the reported amount. This resulted in the SFC issuing a notice under Section 183 of the SFO requiring Sound Global to produce bank statements and information relating to the Group's bank balances and cash positions as at 31 December 2012 and 31 December 2013.

In a separate incident, a discrepancy of about RMB 2 billion was discovered between the balances in the Group's bank accounts at Hua Xia Bank and the information provided previously by Sound Global's management (the **2015 Cash Discrepancy**). Wen's explanation (which was substantiated by an independent review committee and a forensic accounting exercise) was that the sums had been used for "negotiating several acquisitions carried on by his associated companies on behalf of the Group as it was inconvenient to involve the Company due to the scale of the acquisitions".<sup>1</sup> The payments were not recorded in the Group's accounts. The negotiations for the acquisitions subsequently failed, but the funds were not repaid to Sound Global.

Later that year Sound Global produced bank statements and information relating to the bank balances and cash positions, prepared by the Group, as required under the Section 183 notice issued by the SFC. The information provided was found to be inconsistent with that provided to the SFC by the China Securities Regulatory Commission.

## **Section 214 of the Securities and Futures Ordinance**

Section 214(1) of the SFO allows the SFC to apply to the Court of First Instance to make various orders set out in Section 214(2) where it appears to the SFC that the business or affairs of a Hong Kong-listed company have been conducted in a manner:

- (a) oppressive to its members or any part of them;
- (b) involving defalcation, fraud, misfeasance or other misconduct towards its members or any part of them;
- (c) resulting in its members or any part of them not having been given all the information with respect to its business or affairs that they might reasonably expect; or
- (d) unfairly prejudicial to its members or any part of them.

Where the Court of First Instance considers that a listed company's business or affairs have been conducted in a manner described in Section 214(1), it can grant any of the orders listed in Section 214(2) which include:

- any order the court considers appropriate, whether for regulating the conduct of the business or affairs of the company in future, or for the purchase of the shares of any members of the company by other members of the company or by the company (Section 214(2)(e)); and
- an order that a person wholly or partly responsible for the company's business or affairs having been so conducted shall not be, or continue to be, a director or in any way be involved, directly or indirectly, in the management of any listed company for a period of up to 15 years.

## **Findings of the Court of First Instance**

The Court of First Instance first needed to be satisfied that the business or affairs the subject of the proceedings fall within one or more of the heads of misconduct specified in Section 214(1)(a) to (d) (as described above). It found that the business and affairs of Sound Global were conducted by Wen in a manner within Section 214(1)(b), (c) and (d) of the SFO since:

- the schemes and false explanations constituted fraud perpetrated on Sound Global and its subsidiaries which amounted to misfeasance or misconduct within the meaning of Section 214(b) of the SFO;
- the false explanations given in relation to the 2015 Cash Discrepancy constituted misfeasance or misconduct under Section 214(b) of the SFO;
- the schemes and the giving of false explanations resulted in Sound Global's members not having been given all the information with respect to the Group's business and affairs that they might reasonably expect under Section 214(c) of the SFO; and
- the schemes and the giving of false explanations were unfairly prejudicial to Sound Global and its members under Section 214(d) of the SFO given that the Group's financial position had been grossly overstated leaving the true position unknown. Sound Global and its members were also prejudiced by the fact that trading in Sound Global's shares had been suspended since April 2016.

## **Share Purchase Order under Section 214 of the Securities and Futures Ordinance**

The SFC sought an order requiring Wen to make an offer to purchase the shares held by the other members of Sound Global under Section 214(e) of the SFO. That Wen was a member of Sound Global was not in dispute. The court noted that there was no requirement on the part of the SFC to establish that Wen received any financial gain or that Sound Global or its members suffered any loss. Nor was there any requirement to prove that the gain or loss was quantifiable and caused by the misconduct.

The Court stated that in deciding whether to make a share purchase order, it would consider (among others):

- (i) whether there is a lesser remedy that can sufficiently deal with the unfairly prejudicial conduct and there is no likelihood of the conduct being repeated;

- (ii) whether there are difficulties or impracticalities in framing orders for regulating the company's affairs in future or to remedy the misconduct;
- (iii) whether other members of the company would otherwise be locked in the company due to difficulties in disposing of the shares;
- (iv) whether the person against whom the order is sought: (a) was in control of the company at the material time of the misconduct and his interests in the company; (b) acted in clear disregard of the interests of the minority shareholders; and (c) acted in breach of the Listing Rules and other applicable regulations; and
- (v) whether the person against whom the order is sought has the financial means to comply with the order.

Applying these principles, the Court considered it appropriate for it to make an order for Wen to purchase the shares held by Sound Global's other members. The schemes and the 2015 Cash Discrepancy resulted in the financial state of Sound Global and the Group being unclear. The disappearance of all relevant personnel and documents meant that it was impossible for the SFC and Sound Global to ascertain the full extent of the wrongs done to the Group and the extent of any financial loss. The prejudice suffered by Sound Global and its members was considered by the Court to be substantial and irreversible. The Court found that there was no lesser remedy that could be imposed to remedy the situation. The Court also found no evidence that Wen did not have the financial means to purchase the shares of the other members. Objections on the ground that Sound Global's second largest shareholders appeared to be institutional investors were without basis as the SFC merely sought an order for Wen to make an offer to purchase.

## **Disqualification of Wen**

The Court ordered a disqualification of 12 years due to the very serious nature of the misconduct which involved fraud and dishonesty on the part of Wen who had caused, directed and orchestrated the schemes for more than two years. The fact that he provided false explanations of the 2015 Cash Discrepancy to the regulatory authorities, Sound Global's audit committee, auditors and members was also highly prejudicial to Sound Global and its members as it resulted in its shares being suspended from trading for an extended period. Sound Global had also incurred substantial costs in engaging entities to investigate the various transactions as required by its audit committee and the regulatory authorities. That Wen had caused or allowed all relevant personnel and documents to become unavailable was also taken into account in determining the period of disqualification.

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[1] *Securities and Futures Commission v Sound Global Ltd and Others* [2022] HKCFI 3025. 35

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