Application No. 3 of 2007

IN THE SECURITIES AND FUTURES APPEALS TRIBUNAL

IN THE MATTER OF a Decision made by the Securities and Futures Commission under section 116 (6) of the Securities and Futures Ordinance, Cap. 571

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

BETWEEN

SBI E-2 CAPITAL (HK) LIMITED — Applicant

and

SECURITIES AND FUTURES COMMISSION — Respondent

Tribunal: Hon Mr Justice Stone, Chairman

Date of Hearing: 23 April 2007

Date of Determination: 23 April 2007

Date of Reasons for Determination: 17 May 2007

REASONS FOR DETERMINATION

The application

1. By letter dated 5 February 2007 from its solicitors, M/s Arculli Fong & Ng, the applicant herein, SBI E2-Capital (HK) Ltd (hereafter 'SBI') sought review by this Tribunal of a decision of the Director of Licensing of the SFC, as contained in a Notice of Decision and Statement of Reasons dated 15 January 2007, whereby the SFC imposed a Condition on the terms of the applicant's licence in respect of Type 6 regulated activity under section 116(6) of the Securities and Futures Ordinance, Cap 571.

2. The Condition thus imposed was in the terms following: "For Type 6 regulated activity, with effect from 1 January 2007, the [Applicant] shall not act as sponsor in respect of an application for the listing on a recognized stock market of any securities."

3. SBI is dissatisfied with the imposition of such Condition, hence these proceedings, the hearing of which, with the consent of the parties, was conducted by the Tribunal consisting of the Chairman sitting alone, pursuant to the provisions of section 31, Schedule 8, of the SFO, Cap 571.

4. Immediately upon the conclusion of the hearing of this review, the Tribunal dismissed this application, with costs to the respondent, for reasons subsequently to be given.

5. These are those reasons.

The new 'Sponsor Guidelines'

6. Since this is the first case to have come before this Tribunal upon the issue of the application of the 'Additional Fit and Proper Guidelines for Corporations and Authorized Financial Institutions applying or continuing to act as Sponsors and Compliance Advisers' – in general parlance happily reduced to the title 'Sponsor Guidelines' – it may assist to set out a little of the background to these Guidelines.

7. In an SFC Press Release dated 10 April 2006 new eligibility criteria and ongoing obligations for sponsors were announced with the aim of raising sponsor standards in Hong Kong, and hence the promotion of higher standards of corporate governance and market behaviour.

8. Such new Guidelines represented the culmination of a two-stage initiative of the SFC and the Stock Exchange of Hong Kong, and sought to regulate sponsors and compliance advisers more effectively in two particular aspects: first, only those corporate advisory firms that met stringent eligibility criteria might act as sponsors, and second, the SFC was to inspect sponsors and compliance advisers regularly to review compliance.

9. The promulgation of the new Sponsor Guidelines came after a bout of public consultation on the issue of tightening the regulation of sponsors, in the course of which the SFC received 14 submissions from market practitioners, professional bodies and individuals; these responses,

the SFC reported, indicated general support for the proposal to impose specific eligibility criteria and ongoing compliance obligations.

10. Consequent upon such public consultation the SFC set out details of the proposals in a document intituled 'Consultation Conclusions on the Consultation Paper on the Regulation of Sponsors and Compliance Advisers'.

11. The requirements set out therein were introduced as the new 'Sponsor Guidelines', which came into effect on 1 January 2007.

12. These Guidelines constituted an elaboration of, and addition to, the existing Fit and Proper Guidelines, the Guidelines on Competence, and the Code of Conduct for Persons Licensed by or Registered with the SFC. The Explanatory Notes to the new Guidelines note that these other codes and guidelines are "not diminished in any way" by the more specific requirements set out in the Sponsor Guidelines.

13. The document containing these new Guidelines is of some length and contains considerable detail. For present purposes, however, several provisions require highlighting:

- A sponsor should have at least two Principals at all times (para 1.3.1);
- A Principal should meet the eligibility criteria for Principals as set out in section 1.4 of the Sponsor Guidelines, which imposed three requirements: that an individual should be a Responsible Officer of the licensed corporation his licence is accredited to

(para 1.4.1(1)), he should have a minimum of 5 years of relevant corporate finance experience in respect of companies listed on the Main Board and/or GEM Board, and in the five years immediately preceding his appointment, he should have played a substantial role in advising a listing applicant as a sponsor in at least two completed IPO's on the Main Board and/or GEM Board (paras 1.4.1(2) & (3));

- The Management of the sponsor should ensure that the firm has the relevant expertise and resources to perform its role as a sponsor properly (para 1.1.2);
- The Management of the sponsor should ensure that there are sufficient Principals engaged in a full-time capacity to discharge its role in supervising the Transaction Teams (para 1.1.6);
- The level of human resources and expertise should be commensurate with the volume, size, complexity and nature of the sponsor work that is undertaken by a sponsor (para 1.1.6).

The present case: the factual background

14. The applicant, a Hong Kong subsidiary of a Cayman Islands holding company, by letter dated 27 September 2006 notified the SFC that it intended to continue sponsor work after 1 January 2007, and had lodged its submission to demonstrate that it met the 'eligibility criteria' within the new Sponsor Guidelines.

15. By its Letter of Mindedness dated 15 December 2006 the SFC indicated that it was minded to impose a condition on the applicant's licence restricting it from acting as a sponsor for the reasons that: first, one of the

two proposed Principals (who then were identified as Mr Yan and Mr Wan) did not meet the eligibility criteria, and second, that the applicant had not demonstrated that it had reviewed its internal systems and controls.

16. This latter issue, that of internal systems and controls, in fact ceased to be of relevance in the context of this application because the applicant subsequently satisfied the SFC that it had carried out the necessary review.

17. The Letter of Mindedness as issued by the SFC had notified the applicant of its right to be heard under section 140 of the SFO, and had invited the applicant to set out its grounds, if any, for objecting to the condition proposed before 29 December 2006.

18. The applicant duly replied by letter dated 20 December 2006 which contained its representations consequent upon the Letter of Mindedness.

19. This reply dealt only with the 'internal controls' issue which had been raised – which issue, of course, subsequently was resolved.

20. However, the applicant in its response did *not* take issue with the SFC objection to one of the Principals as earlier named, but simply said that the applicant recently had submitted an application to the regulator to have a Mr Simon Harding approved as a Responsible Officer and Principal of the Applicant: Mr Harding currently was an RO of SBI Crosby Ltd, a company within the same group as the applicant, the applicant concluding

that “in this regard were are of the view that we meet the eligibility criteria for principals under paragraphs 1.3 and 1.4 of the Sponsor Guidelines.”

21. In fact, this application with regard to Mr Harding was properly lodged on 22 December 2006, and on the same date the applicant also applied to have a Mr Lee Deng Charng approved as a Responsible Officer and Principal of the applicant.

22. It is a matter of record that the two Principals as originally proposed, namely Messrs Yan and Wan, had resigned before the SFC had reached a final decision on the applicant’s submission, and thus the SFC took the view that, if the applicant’s sponsor submission were to be approved, both the proposed new Principals, Messrs Harding and Lee, currently should be eligible to be Principals.

23. However, so far as the SFC was concerned, this was not the case.

24. Notwithstanding that for the purpose of the Sponsor Guidelines the applicant had declared that it was satisfied that Messrs Harding and Lee were qualified to act as Principals, factually this was not then the position: whilst applications indeed had been made for these gentlemen to be made Responsible Officers of the applicant, no decision yet had been made on this issue, and thus at the relevant time of making its sponsor submission the applicant did not have in place two eligible Principals.

25. Moreover, whilst in terms of the applications nominating Messrs Harding and Lee as Principals the applicant had declared that they would discharge their roles in supervising the transaction team "in a full time capacity", the SFC considered that this could not be the case in that these gentlemen already were nominated to act as Principals of the sister subsidiary SBI Crosby Limited.

26. The regulator thus took the view that even were Messrs Harding and Lee duly to be approved as RO's of the applicant, the applicant's management could not and were not in position to ensure that there were sufficient Principals engaged in a full-time capacity in order to discharge the supervision of Transactions Teams.

27. Consequent upon this correspondence with the applicant, the SFC issued its Notice of Decision and Statement of Reasons dated 15 January 2007 imposing the licence condition of which complaint now is made. The SFC made it clear in its Statement of Reasons that all the information provided by the applicant in response to the Letter of Mindedness had been taken into account.

The argument

28. Against this historical backdrop, Mr Simon Yung of the solicitors representing the applicant advanced an argument that, at bottom, rested upon two basic submissions.

29. First, it was argued that there was failure on the part of the SFC to interpret the new Sponsor Guidelines reasonably, taking into account the applicant's circumstances as a whole.

30. In this context Mr Yung referred to the broad corporate structure, and the fact that both the applicant and SBI Crosby were within the SBI E2-Capital Group, with a common Cayman Islands holding company, SBI E2-Capital Ltd. He noted that the applicant and SBI Crosby shared the same office premises and support staff, and further that it was anticipated that there would be an imminent merger, and that the business of SBI Crosby would be wound down and its professional personnel ultimately transferred to the applicant.

31. Mr Yung also submitted that the interpretation accorded to the term 'full-time' by the SFC was overly restrictive and narrow, and that in the circumstances this should be accorded a more purposive and wider interpretation consistent with the circumstances – and potential circumstances – of the applicant and SBI Crosby. He further said that it was unclear why the application by Mr Harding for RO accreditation had been approved as early as January 2007, whilst Mr Lee's application had not yet been granted, despite being filed shortly after that of Mr Harding.

32. The second basic submission raised by Mr Yung was that which he termed 'procedural impropriety' on the part of the SFC, which in this context he took to connote the "hasty conclusion" reached by the regulator as to the applicant's sponsor submission, coupled with the "lack of an in-depth view" of the requirement within the Guidelines (at para 1.1.6)

regarding the commensurate nature of the level of human resources and expertise when compared with the volume, size, complexity and nature of the sponsor work undertaken by the sponsor.

33. In this regard Mr Yung asserted that the Sponsor Guidelines should be interpreted with a "high degree of consistency" and with the intention of producing a result "that is able to stand the fair and reasonable test".

34. On behalf of the SFC, Ms Coupe strongly resisted these submissions.

35. In essence she relied upon the applicant's current and clear failure to meet the eligibility criteria in the Sponsor Guidelines, and further suggested – with, it seems to me, some justification – that it was a bit rich for the applicant, through its solicitor, now to be contending that the SFC had not taken into account the matters now relied upon when the unvarnished fact was that the arguments now marshalled were raised only *after* the SFC decision in the matter had been issued, and had not been included in the representations made by the applicant in response to the Letter of Mindedness.

36. In my view, however, the latter is essentially a costs' point and does not preclude the applicant now from making its arguments on this review in opposition to the decision of which complaint is made.

Reasons for Determination

37. In my judgment this was not an application meriting extensive reflection, and consistent with that view this Tribunal dismissed the application, with costs, immediately upon the conclusion of argument.

38. Although Mr Yung said all that could be said on his client's behalf, I did not consider that this application had any residual merit.

39. The application as mounted also struck me as premature. It seemed to me that in so far as the applicant's submissions reflected the possibility of imminent corporate changes, in terms, for example, of the proposed merger and transfer of professional personnel from SBI Crosby to the applicant, and in terms of the likely result of the currently-extant application of Mr Lee for RO status, that these were matters which would (or possibly would not) resolve themselves, but that if such resolution enured to the advantage of the applicant, it was at least a possibility that the existing difference of view with the regulator would be resolved. Nevertheless, when this temporal aspect was raised by the Tribunal, Mr Yung rejected the suggestion and declined to canvass the possibility of an adjournment, doubtless because his brief was to attempt to remove the disputed licence condition with immediate effect.

40. That he was unable to achieve this was because in the circumstances I took the view that this application by SBI represented no more than an exercise in special pleading.

41. There is no question but that on the facts as presently existing the applicant had failed to meet the specific eligibility criteria within the Sponsor Guidelines: the applicant did not have two eligible Principals because the only proposed Principals, that is, Messrs Harding and Lee, were not Responsible Officers of the applicant, and, as Ms Coupe pointed out, in fact that remained the position as at the date of this review hearing.

42. Nor do I accept the contention on the part of the applicant that "it should be acceptable" for these two gentlemen to be Principals *both* of the applicant and of SBI Crosby, since these companies are part of the same group, and that the applicant and SBI Crosby are currently working on one active sponsor case so that Messrs Harding and Lee would have "adequate capacity" to supervise the applicant's sponsor work. I quite fail to appreciate how it should be thought that the market regulator in the active (and volatile) market of present day Hong Kong should be required to make a serious compliance decision on the basis of the perceived current workload of a sister company of the applicant, which is the sum total of this submission.

43. Moreover, in this regard I accepted the SFC argument to the effect that the role of Principal as defined in the Sponsor Guidelines, namely, to be in charge of the supervision of the Transaction Teams, which in turn involves the making of key decisions (as, for example, the breadth and depth and acceptability of any 'due diligence' review in any particular case), is such that the SFC is entitled to take the view that a Principal can properly discharge his supervisory responsibilities in respect of one sponsor firm only – a stance which is reflected in the Guideline (at para 1.3.1) as to the

"full time capacity" of the Principal in order to discharge the role of supervision of the Transaction Teams.

44. In making the decision to dismiss this application I accorded little weight to the ambitious submission that apparently there is a "plan" that the sponsor business of SBI Crosby will be wound down in or around mid-2007, and that thereafter its professional staff will transfer to the applicant.

45. This is interesting, but at present it counts for naught. Corporate 'plans' notoriously are susceptible to change (in many instances doubtless for good commercial reasons), and it seems to me that the fact that this is being anticipated, or is in the pipeline, is nothing to the immediate point.

46. In this context the objective observer might rhetorically ask why, in considering sponsor submissions, the SFC apparently should be required to take into account the possibility of future events, as opposed to acting and deciding on the basis of indisputable existing fact?

47. The answer to this seems to me to be obvious: in conducting its regulatory affairs the SFC is *not* to be required to utilize a crystal ball, and in any event, as Ms Coupe observed, if and in so far as the proposed 'merger plan' is indeed implemented, it remained open to the applicant to have the existing licence condition removed at a time when it can demonstrate that it is in compliance with the existing Sponsor Guidelines.

48. Alternatively, as indeed the Tribunal suggested to Mr Yung during argument, given that the initially proposed Principals, Messrs Yan and Wan, themselves clearly had been 'hired away', the option currently open to the applicant, if indeed it could not wait for such merger to be effected, would be itself to go into the market and to hire appropriate personnel to render the applicant 'Sponsor Guideline compliant' in terms of the existence of two full time Principals, rather than, as now is the case in this application, proceeding to criticise the SFC for refusing to accept the applicant's suggested compromise of the Sponsor Guidelines, the specific terms of which the regulator has a clear obligation to the market to uphold and to apply.

49. The additional argument was made on behalf of the applicant that, in all the circumstances of this particular case, the SFC was in error in failing to exercise its discretion to grant a dispensation from the eligibility criteria, as is provided for in the Note to para 1.4.1 of the Sponsor Guidelines.

50. To this Ms Coupe's response was that first, the applicant had not applied for such a dispensation, and second, and in any event, she submitted that a dispensation could only be sought in relation to the eligibility requirement for Principals (eg., the 'RO'/experience requirement), and not for the general requirement that the sponsor must have adequate resources including at least two Principals who are engaged in a full-time capacity.

51. In my view this submission was well-founded.

52. What the applicant appears to have done is to make application under section 134 of the SFO for a modification or waiver of condition, (which application, at least on the face of the correspondence, appears to be ongoing and has not yet been decided), and as I understand the position this is not the same as an application for dispensation of the eligibility requirement for Principals (as contained within the Note to para 1.4 of the Sponsor Guidelines) which seems not to have been mounted. Moreover, Ms Coupe appears correct in her suggestion that any such potential dispensation is relevant only to eligibility criteria.

53. It follows, therefore, that from the applicant's point of view there was nothing in this submission either; moreover, if and in so far as the applicant in fact had applied for such a dispensation, then it is highly unlikely that this Tribunal would have seen fit to interfere with a good faith exercise of an SFC discretion in this regard.

54. Which brings me to a repetition of a broad point which has been the subject of frequent Tribunal comment in past Determinations, and I make the point again because regrettably it appears that such earlier observations do not appear to have been heeded. It is this.

55. This Tribunal is *not* a regulator. It neither has the skill, knowledge nor, I apprehend, the patience.

56. It exists solely as a supervisory body to ensure correctness in law and fairness of process, to remedy manifest errors, and occasionally (and

fortunately rarely) to act as an arbiter of allegations of bad faith and/or capriciousness.

57. This Tribunal does *not* exist simply in order to substitute its own judgment for that of the regulator when the regulator, on the basis of all available and relevant information, in good faith has made a considered judgment or reached a conclusion or exercised a regulatory discretion, and it must be re-emphasized that any application for review which merely seeks to achieve contrary result, absent the existence of clear and discernible error, is doomed to fail.

58. This is not a new principle. In a very early case, *SFAT No 2 of 2003, Application by Wong Pui-hey, Duncan,* this Tribunal was minded to make the following observation:

> "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."

59. There has been no change in primary approach since that was said, but surprisingly applications such as the present continue to be launched when it is as plain as a pikestaff that the complaint in issue amounts to no more than dislike of or antipathy to the regulatory decision in question rather than genuine complaint as to misuse of process and/or the perpetration of unfairness and/or the making of clear and obvious error.

60. Why in the instant case it should have been thought that the Tribunal would have chosen to interfere with an SFC decision obviously carefully made in light of undisputed facts, and within the application of proper principle, is not clear. All that has been achieved by this exercise, it seems to me, is a waste of judicial time and the wholly unwarranted expenditure of not inconsiderable costs.

61. It is thus for the foregoing reasons that this Tribunal took the view that no grounds had been established which cast doubt upon the legitimacy or propriety of the exercise by the SFC of the power in section 116(6) of the SFO to impose the licence condition, and as a consequence dismissed the application for review, and confirmed the SFC decision in question.

Hon Mr Justice Stone
(Chairman)

Mr Simon Yung of Messrs Arculli Fong & Ng, for the applicant

Ms Elizabeth Coupe, Senior Counsel Legal Services Division of the SFC, for the respondent