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Citation: Sino-Forest Corporation (Re), 2018 ONSEC 37  
Date: 2018-07-09

**IN THE MATTER OF  
SINO-FOREST CORPORATION, ALLEN CHAN, ALBERT IP, ALFRED C.T. HUNG,  
GEORGE HO, SIMON YEUNG and DAVID HORSLEY**

**REASONS AND DECISION ON SANCTIONS AND COSTS  
(Sections 127 and 127.1 of the *Securities Act*, RSO 1990, c S.5)**

**Hearing:** November 20 and 27, 2017  
January 18, 2018  
March 26 and 27, 2018

**Decision:** July 9, 2018

**Panel:** D. Grant Vingoe Vice Chair and Chair of the Panel  
Deborah Leckman Commissioner  
Garnet W. Fenn Commissioner

**Appearances:** Hugh Craig For Staff of the Commission  
Carlo Rossi

Adam D.H. Chisholm For Allen Chan, Albert Ip, Alfred C.T.  
Jeffrey Levine Hung, George Ho and Simon Yeung  
Jon Wypych

No one appeared on behalf of Sino-Forest Corporation.

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## REASONS AND DECISION

### I. INTRODUCTION

- [1] Sino-Forest described itself as a leading commercial forest plantation operator in China. Sino-Forest became a reporting issuer in Ontario in 1995 when it listed its shares on the TSX through a reverse takeover transaction. Between February 2003 and October 2010 Sino-Forest raised approximately US \$3 billion from investors by issuing debt and equity securities. From June 30, 2006 to March 31, 2011, Sino-Forest's share price rose 340% from CA \$5.75 to CA \$25.30.
- [2] On June 2, 2011, the Muddy Waters Report<sup>1</sup> was released alleging Sino-Forest was a "near total fraud" and a Ponzi scheme. The day before the Muddy Waters Report was released, Sino-Forest's share price was CA \$18.21. By June 21, 2011, the share price had declined to CA \$1.99.
- [3] On August 26, 2011, the Commission ordered all trading in Sino-Forest shares to cease.
- [4] On May 9, 2012 the TSX delisted Sino-Forest shares.
- [5] In May 2012, Staff commenced this proceeding against Sino-Forest and the individual respondents – Allen Chan, Albert Ip, Alfred Hung, George Ho, Simon Yeung and David Horsley – alleging misconduct during the Material Time: June 30, 2006 to January 11, 2012.
- [6] On January 30, 2013, Sino-Forest entered a Plan of Compromise and Reorganization that resulted in Sino-Forest's former bondholders transferring all of its remaining assets into Emerald Plantation Holdings. Emerald assigned a nil value to the BVI standing timber assets, a central portion of Sino-Forest's total reported assets and source of revenues.
- [7] David Horsley, Sino-Forest's former CFO, settled the proceeding brought by Staff of the Commission against him prior to the start of the Merits Hearing.
- [8] The hearing to determine whether the remaining respondents engaged in the misconduct alleged by Staff began on September 2, 2014. The Merits Hearing was exceptionally long. It lasted 188 days and involved over 2000 exhibits. Twenty-two witnesses testified in Toronto, Hong Kong, mainland China and the Dominican Republic, some through video conferencing. Mr. Chan did not testify.
- [9] The Merits Decision was issued on July 13, 2017.<sup>2</sup> The Merits Panel found that during the Material Time the respondents perpetrated one of the largest corporate frauds in Canadian history. With deliberate planning and foresight, the respondents constructed an elaborate and complex organizational structure that misled investors and resulted in the cumulative loss of CA \$6 billion in equity market capitalization, separate and apart from losses affecting Sino-Forest's outstanding debt.
- [10] We must determine the appropriate sanctions and costs order given the Merits Panel's findings.

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<sup>1</sup> Unless defined in these Reasons and Decision, initially capitalized terms used in these Reasons and Decision have the meanings assigned to them in the Merits Decision.

<sup>2</sup> *Sino-Forest Corporation (Re)*, 2017 ONSEC 27, 40 OSCB 6291.

- [11] Staff seek an order imposing prohibitions, administrative penalties, disgorgement and costs on Allen Chan, Albert Ip, Alfred Hung and George Ho. Staff seek an order imposing prohibitions and an administrative penalty on Simon Yeung, but do not seek disgorgement and costs. Staff do not seek any sanctions against or costs from Sino-Forest.
- [12] The respondents and Staff agree on the prohibitions to be ordered, but disagree on the appropriate administrative penalties and orders for disgorgement.
- [13] The respondents and Staff also agree on the appropriate amount of costs to be ordered.

## **II. THE INDIVIDUAL RESPONDENTS**

- [14] Allen Chan was a co-founder of Sino-Forest in 1992 and Chairman of the Board and CEO during the Material Time until his resignation on August 28, 2011. Mr. Chan was born, educated and resided in Hong Kong and had extensive relationships at both the local and central levels of the Chinese government. Mr. Chan was very involved in day-to-day operations. For example, he approved every purchase contract and signed every sales contract in the BVI Model, in which Sino-Forest used subsidiaries incorporated in the British Virgin Islands. Mr. Chan was the ultimate decision maker and compensating control; he was regarded as a 'visionary', deciding Sino-Forest's direction, strategy and goals. No significant decisions were made without Mr. Chan's knowledge and approval.
- [15] Albert Ip was the Senior Vice President, Development and Operations North-East and South-West China and reported directly to Mr. Chan. Mr. Ip was in charge of operations for 48 subsidiaries and supervised over 1000 employees with operations distributed over nine provinces across Mainland China. Within the BVI Model, Mr. Ip was responsible for standing timber purchases. He worked at Sino-Forest from 1997 until March 30, 2012. Mr. Ip obtained an engineering degree from the University of Ottawa in 1984.
- [16] Alfred Hung was Vice-President Corporate Planning for Sino-Forest for much of the Material Time, joined Sino-Forest in 1999, and reported to Mr. Chan. Within the BVI Model, he oversaw the drafting of purchase and sales contracts and the netting of accounts receivable and accounts payable. His central role was critical to the Deceitful Documentation Process. Mr. Hung was a member of the Disclosure Committee. He received a Masters of Finance, an MBA, and a Financial Risk Manager designation. Mr. Hung lost his professional designation as a Chartered Financial Analyst as a result of his breaches of the *Securities Act*, RSO 1990, c S.5 (the **Act**).
- [17] George Ho joined Sino-Forest in 2007 and was Vice-President, Finance for Sino-Forest and CFO and Vice-President Finance of Sino-Panel, the holding company for the BVI Model. He had ultimate oversight over accounting personnel at Sino-Panel and reported directly to Mr. Chan. He obtained a Bachelor of Commerce degree in accounting from Simon Fraser University and worked at business and accounting firms in Canada and Hong Kong prior to joining Sino-Forest.
- [18] Simon Yeung was Vice-President, Operations of Sino-Panel, having joined Sino-Forest in 2002, and reported to Mr. Ip. He was described as a "first line trouble shooter to deal with operational issues." Mr. Yeung obtained a degree in economics and a mechanical engineering diploma.

### **III. THE MERITS DECISION**

[19] The Merits Panel found that:

- a. Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho committed fraud through their participation in elements of the Standing Timber Fraud, which resulted in the overstatement of Sino-Forest's assets and revenue.
- b. Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho authorized, permitted and/or acquiesced in Sino-Forest making disclosures which were misleading in a material respect regarding Sino-Forest's assets and revenue, the effects of the fraud on reported revenue, and Sino-Forest's internal controls.
- c. Mr. Chan committed fraud in connection with the Greenheart Transactions, by concealing his interest in Greenheart when it was purchased by Sino-Forest.
- d. Mr. Chan authorized, permitted and acquiesced in Sino-Forest making disclosures that were misleading in a material respect regarding his interest in Greenheart.
- e. Mr. Chan, Mr. Ip, Mr. Ho, Mr. Hung and Mr. Yeung misled Staff during the investigation.

[20] Given the length of the Merits Decision, we summarize below the Merits Panel's findings in more detail.

#### **A. The Standing Timber Fraud**

[21] The Merits Panel found that the Standing Timber Fraud was an elaborate scheme to defraud investors, and that Mr. Chan, Mr. Ip, Mr. Ho and Mr. Hung knew their conduct was deceitful and dishonest and put investors' pecuniary interests at risk.

[22] There were three elements necessary to perpetrate the Standing Timber Fraud: undisclosed control of purportedly independent third parties; the deceitful documentation process; and internal control weaknesses.

[23] Mr. Chan engaged in all three elements of the Standing Timber Fraud during the Material Time, which ultimately caused the assets and revenue derived by the purchase and sale of standing timber to be fraudulently overstated and put the pecuniary interests of investors at risk. Not only was Mr. Chan intimately involved in virtually every aspect of the Standing Timber Fraud during the Material Time, as CEO, he was regarded as Sino-Forest's 'visionary', setting the 'tone at the top', and determining Sino-Forest's long term strategy. Mr. Chan engaged in deceitful and dishonest conduct related to Sino-Forest's standing timber assets and revenue that he knew constituted fraud, contrary to subsection 126.1(b) of the Act, and contrary to the public interest.

[24] Mr. Ip was also found to be intimately involved in virtually every aspect of the Standing Timber Fraud during the Material Time. He knowingly deceived investors through his involvement in Sino-Forest's undisclosed control of companies and in the Deceitful Documentation Process. These two elements independently harmed investors by putting their pecuniary interests at risk. Mr. Ip's oversight of the execution of all Four Frauds – four examples of the Standing Timber Fraud considered by the Merits Panel – demonstrates the oversight he had over Sino-Forest's fraudulent operations. Mr. Ip directed employees of the

Sino-Panel Group in the fraudulent recording of transactions in the Four Frauds that led to Sino-Forest's overstatement of assets and revenue during the Material Time. Mr. Ip engaged in deceitful and dishonest conduct related to Sino-Forest's standing timber assets and revenue that he knew constituted fraud, contrary to subsection 126.1(b) of the Act, and contrary to the public interest.

- [25] Mr. Hung was the central figure in, and controlled, the Deceitful Documentation Process which put investors' pecuniary interests at risk. He knew his role in the internal control weakness resulting from the concentration of duties was a key element of the Standing Timber Fraud, and went along with Mr. Chan's failure to remediate this internal control weakness. Mr. Hung engaged in deceitful and dishonest conduct related to Sino-Forest's standing timber assets and revenue that he knew constituted fraud, contrary to subsection 126.1(b) of the Act, and contrary to the public interest.
- [26] Mr. Ho knowingly deceived investors through his involvement in Sino-Forest's undisclosed control of companies with which it transacted business. This element of the Standing Timber Fraud, on its own, put the pecuniary interests of investors at risk. Although Mr. Ho was not an architect of the Deceitful Documentation Process in the way Mr. Chan, Mr. Ip and Mr. Hung were, his involvement in three of the Four Frauds demonstrates he nonetheless played a significant role in the Standing Timber Fraud. Mr. Ho engaged in deceitful and dishonest conduct related to Sino-Forest's standing timber assets and revenue that he knew constituted fraud, contrary to subsection 126.1(b) of the Act, and contrary to the public interest.

### **1. Undisclosed Control of or Influence Over Related Companies**

- [27] The Merits Panel found that Sino-Forest controlled, or had significant influence over, customers and suppliers that were purported to be arms' length. None of these relationships were disclosed to investors. Sino-Forest controlled Yuda Wood, its largest supplier between 2007 and 2010, with approximately US \$600 million in transactions, or more than 20% of all BVI transactions during that time period. Sino-Forest controlled Kun'an, Sino-Forest's largest supplier in 2009, with US \$264 million in purchases, or 29% of total BVI purchases in that year. Also found to be controlled by Sino-Forest were Taiyuan and Dongkou. Juncheng, Shunxuan, Yuangao and Meishan were companies over which Sino-Forest exerted significant influence and were related parties.
- [28] This complex web of related and controlled companies was required in order to perpetrate the Standing Timber Fraud. With no independent verification of purchases and sales, the true economic substance of transactions between Sino-Forest and these companies was called into question. Similarly, the existence and value of assets and revenues recorded in the financial statements was called into question.
- [29] Through the resulting misleading disclosure, Sino-Forest deceived investors about the accuracy and reliability of its financial statements. Investors could not make informed decisions to buy, sell or hold Sino-Forest securities. Investors relied on the completeness and accuracy of Sino-Forest's statements, and were misled.
- [30] Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho deliberately hid information from Sino-Forest's Audit Committee, Board of Directors and auditors about the nature of

Sino-Forest's relationships with these companies. As Chairman and CEO, Mr. Chan was involved in, and ultimately responsible for, the company's disclosure. He knew the importance of providing complete and accurate disclosure to investors, yet he intentionally hid key information concerning undisclosed control. He knew the disclosure was deceitful and put the pecuniary interests of investors at risk.

- [31] Mr. Ip was responsible for all purchases in the BVI Model and oversaw key elements of the business and transactions of companies that were controlled by, or related to, Sino-Forest. Examples of his wide-ranging oversight include his involvement in the supposedly independent audit confirmation process, his oversight of the changing shareholder structure of Yuda Wood's parent company, HK Sonic Jita, and his oversight of bank accounts of many of these controlled or related companies. He understood these relationships were critical to the success of the Standing Timber Fraud. As a senior officer, Mr. Ip certified that the financial statement disclosure was accurate when he knew it was not, and knowingly put the pecuniary interests of investors at risk.
- [32] Mr. Hung was involved in and knew of Sino-Forest's role in the creation of Audit Confirmation Letters, which he knew should have been independent but were not. The purpose of these Audit Confirmation Letters was to provide independent confirmation from Sino-Forest's suppliers and customers to the auditor of their transactions with Sino-Forest.
- [33] Mr. Ho was involved in Sino-Forest's control over related companies. Mr. Ho's approval was required to apply Yuda Wood's corporate chops and make payments from its bank accounts. He was also involved in the supposedly independent audit confirmation process. Mr. Ho knew these companies were not independent of Sino-Forest. He was CFO of Sino-Panel and had ultimate oversight of accounting for the Sino-Panel subsidiaries. He has an accounting background and knew related party transactions would call into question the assets and revenue of Sino-Forest. He sat on Sino-Forest's Disclosure Committee, whose mandate was to assist senior officers in fulfilling their responsibility for oversight of the completeness, accuracy and timeliness of Sino-Forest's disclosures. He certified Sino-Forest's disclosure was accurate when he knew it was not and he took no steps to correct the inaccurate disclosure. The Panel found that Mr. Ho knew concealing this critical information about Sino-Forest's control and related party relationships put investors' pecuniary interests at risk.

## **2. Deceitful Documentation Process**

- [34] The Merits Panel found that the Deceitful Documentation Process was an elaborate scheme involving purchase contracts, Forestry Bureau Confirmations, Survey Reports, sales contracts, set-off documents and audit confirmation letters.
- [35] Mr. Chan, Mr. Ip and Mr. Hung were the key architects of the Deceitful Documentation Process, which put investors' pecuniary interests at risk.
- [36] Mr. Chan was deeply involved and actively participated in the Deceitful Documentation Process. As the "ultimate and compensating control" over transactions and the signatory on all sales contracts in the BVI Model, Mr. Chan's frontline role was not merely ceremonial. He knew key documentation was

missing from purchase contracts and knew the process descriptions relied on by E&Y did not accurately reflect the documentation process. Mr. Chan deliberately hid from the auditors what actually occurred.

- [37] Mr. Chan instructed Mr. Hung to pay suppliers before written contracts were prepared. He also instructed that plantation locations be kept secret in documentation, such that the documentation was insufficient to identify plantation locations. Mr. Chan signed contracts in the quarter following when they were recorded. Notwithstanding this, he certified that the financial disclosure was accurate and complete.
- [38] Mr. Chan knew Sino-Forest's BVI entities could not obtain Plantation Rights Certificates (**PRCs**) and was not even applying for them; he nonetheless authorized the misleading public disclosure that Sino-Forest was applying for PRCs. Mr. Chan failed to disclose the crucial fact that, because BVI entities could not obtain PRCs, Sino-Forest was never the legal and registered owner of the standing timber in the BVI Model. Mr. Chan misled the Board of Directors, the Audit Committee and E&Y about critical information which led to Sino-Forest's inaccurate disclosure, putting investors' pecuniary interests at risk.
- [39] Mr. Ip was intimately involved in the Deceitful Documentation Process through his role in overseeing all purchases in the BVI Model. He approved all purchases and by Q2 2010 was signing all purchase contracts. He was responsible for the Sino-Panel Resource Department, which sourced the BVI standing timber. Like Mr. Chan, Mr. Ip knew BVIs could not obtain PRCs and Sino-Forest was not even applying for them; nevertheless he certified the misleading disclosure to the contrary. Mr. Ip knew the BVI standing timber could not be located. Mr. Ip knew the BVI Model assets and revenue recorded in the financial statements could not be relied upon, which put investors' pecuniary interests at risk.
- [40] Mr. Hung was the central figure in, and controlled, the Deceitful Documentation Process. He certified that Sino-Forest disclosure contained no untrue statement of material facts and did not omit facts necessary to make them not misleading. Mr. Hung knew these financial statements were misleading. Mr. Hung directed the settlement of receivables and payables prior to the existence of contracts. He directed the preparation and backdating of purchase and sales documentation in batches in the quarter following their recognition in financial statements. He was a member of the Disclosure Committee, but took no steps to correct the inaccurate disclosure. Mr. Hung had an extensive educational background in finance and was aware of the consequences of inaccurate disclosure on the pecuniary interests of investors.
- [41] The purchase documentation was fundamentally flawed. Sino-Forest employed the Deceitful Documentation Process whereby Sino-Forest drafted and executed purchase contracts and Forestry Bureau Confirmations in batches in the quarter after they were dated and the assets were recorded. The Merits Panel found that the respondents' convoluted description of the purchase process, based on handshakes, phone calls and sticky notes involving billions of renminbi, was simply unbelievable.
- [42] There is no evidence that ownership of standing timber was ever transferred to Sino-Forest in the BVI Model. Sino-Forest recorded the asset value of its BVI standing timber in its financial statements at US \$1.088 billion in 2007, US

\$1.479 billion in 2008, US \$1.901 billion in 2009 and US \$2.475 billion in 2010. The Merits Panel found that the purchase documentation did not establish proof of ownership and did not identify the location of this standing timber such that its existence could be readily and independently verified. The purchase documentation process was deceitful.

- [43] Similarly, the sales documentation process was fundamentally flawed. Sino-Forest employees employed a deceitful documentation process whereby Sino-Forest drafted and executed sales contracts in batches in the quarter after they were dated and recognized in the financial statements.
- [44] The flawed sales documentation process resulted in Sino-Forest recognizing revenue in the BVI Model in a manner that was deceitful. Sino-Forest recorded revenue from the sale of BVI standing timber of US \$501 million in 2007, US \$644 million in 2008, US \$882 million in 2009 and US \$1.326 billion in 2010. The Merits Panel found the revenue disclosure in the financial statements was inaccurate, did not represent what actually occurred and was therefore deceitful.
- [45] Because BVI subsidiaries could not have bank accounts in Mainland China, Sino-Forest employed a complex set-off process whereby Sino-Forest customers were directed to make payments to Sino-Forest suppliers rather than to Sino-Forest directly. However the process apparently involved layers of third, fourth and fifth customers and suppliers, referred to as a "daisy chain of cash". In effect, Sino-Forest had no way of knowing if accounts payable and receivable were settled, and taxes paid, assuming they were settled at all. In fact, while Sino-Forest had a 100% collection record in the BVI Model prior to the Muddy Waters Report, subsequently, many customers simply deregistered and disappeared, leaving Sino-Forest with US \$887.4 million in uncollectible accounts receivable. No disclosure of the actual set-off process was included in the financial statements, which made the statements incomplete, inaccurate and deceitful.
- [46] Sino-Forest used the Deceitful Documentation Process (purchases, sales and set-offs) to obscure the truth about its ownership of standing timber and standing timber revenue recognition in the BVI Model. This Process deceived investors about the assets Sino-Forest purportedly owned and the revenue recognized from the sale of standing timber. Sino-Forest stated it had proof of ownership when it did not. Sino-Forest created supposedly independent Forestry Bureau Confirmations, which were not proof of legal ownership, and the standing timber could not be located. Sino-Forest misstated its revenue recognition resulting from the sales of standing timber in its public disclosure. The Set-Off Process was a means by which Sino-Forest deceived its auditors and investors about the volume and value of transactions in the BVI Model.
- [47] The Deceitful Documentation Process called into question the assets and revenue Sino-Forest recorded in the BVI Model during the Material Time, significantly putting the pecuniary interests of investors at risk. Approximately 70% of the total timber holdings by hectare and approximately 70% of the revenue the company recognized between 2007 and 2010 could not be verified. In the six years that passed between the Muddy Waters Report and the end of the Merits Hearing there was no evidence that demonstrated the ownership or existence of the BVI assets that had been valued at CA \$2.9 billion on Sino-Forest's 2010 financial statements. The complexity, scale and duration of the fraud are simply stunning.

### **3. Undisclosed Internal Control Weaknesses**

- [48] The Merits Panel found that the concentration of duties in Mr. Hung was an essential element of the Standing Timber Fraud. Mr. Hung's role encompassed recording BVI standing timber purchases and sales, reporting the information to Sino-Forest's accounting department, providing all supporting documentation and settling all accounts receivable and payable in the BVI Model.
- [49] The Merits Panel found that Mr. Chan could have easily remediated this internal control weakness, but did not, because it facilitated the continuation of the Deceitful Documentation Process. He misled the Board when he claimed remediating this concentration of control would jeopardize relationships with customers and suppliers because Mr. Hung had no relationships with them. Mr. Chan dishonestly concealed the lack of segregation of duties in Sino-Forest financial statement disclosure. Mr. Chan's motivation in perpetuating the lack of segregation of duties was to maintain the Standing Timber Fraud. Mr. Hung knew the significance of this internal control weakness and went along with Mr. Chan's failure to remediate it.

### **4. Four Examples of The Standing Timber Fraud – The "Four Frauds"**

- [50] The Merits Panel found that the respondents collectively engaged in fraud in respect of four sets of transactions – the Four Frauds – that were used by Staff to illustrate the Standing Timber Fraud: the Dacheng Transactions, the 450 Transactions, the Gengma #1 Transactions and the Gengma #2 Transactions.
- [51] The Dacheng Transactions provide an example of Mr. Ip and Mr. Ho's involvement in the perpetration of the Standing Timber Fraud. In the Dacheng Transactions Sino-Forest recorded the sale of the same assets in the BVI and WFOE Models. The BVI purchase was fictitious and inflated the assets on Sino-Forest's financial statements for 2008 by approximately US \$30 million. The sale of these duplicate assets through the BVI Model was likewise fictitious and resulted in the overstatement of Sino-Forest's revenue in 2009 by approximately US \$48 million. This overstatement of assets and revenue put the pecuniary interests of investors at risk.
- [52] The 450 Transactions provide an example of Mr. Chan, Mr. Ip and Mr. Ho's involvement in the Standing Timber Fraud. The purchase and sales contracts in the 450 Transactions, which were purportedly executed in the same quarter, were reverse-engineered with the full knowledge and support of Mr. Chan, Mr. Ip and Mr. Ho. Documentation to support these transactions was created to deceive Sino-Forest's CFO and auditors. The sales contracts had no economic substance and resulted in Sino-Forest's overstatement of revenue by approximately US \$30 million in 2009. This revenue was found not to exist.
- [53] The Gengma #1 Transactions provide an example of Mr. Chan and Mr. Ip's involvement in the perpetration of the Standing Timber Fraud. Sino-Forest created fictitious purchase contracts in the BVI Model in order to inflate the value of forest assets on its financial statements in 2007, 2008 and 2009. The actual purchase of the plantation was in the WFOE Model. Sino-Forest created fictitious sales contracts that inflated its revenue by US \$231 million in 2010. These assets were never sold by Sino-Forest, thereby overstating revenue by the full amount of US \$231 million.

[54] The Gengma #2 Transactions provide an example of Mr. Chan, Mr. Ip and Mr. Ho's involvement in the perpetration of the Standing Timber Fraud. Sino-Forest created fictitious purchase contracts that inflated the value of assets on Sino-Forest's financial statements in 2007 and 2008, and created fictitious sales contracts that misstated revenue on its financial statements in 2008 and 2009 by approximately US \$49 million.

## **B. Materially Misleading Statements**

[55] The Merits Panel found that Sino-Forest made statements in its Impugned Disclosure Documents issued during the Material Time that were misleading in a material respect. The materially misleading statements relate to: (i) statements regarding ownership of assets and revenue recognition, (ii) the effects of the Four Frauds on the reported revenue of Sino-Forest, and (iii) statements regarding internal controls.

[56] Mr. Chan authorized and permitted Sino-Forest's making of statements that were misleading in a material respect.

[57] Mr. Ip and Mr. Ho permitted and acquiesced in Sino-Forest's making of statements that were misleading in a material respect.

[58] Mr. Hung permitted Sino-Forest's making of statements in respect of ownership of assets and revenue recognition that were misleading in a material respect, and acquiesced in Sino-Forest's making of statements in respect of its internal controls that were misleading in a material respect.

### **1. Statements Regarding Ownership of Assets and Revenue Recognition**

[59] Mr. Chan, as CEO, authorized and permitted the making of materially misleading statements by Sino-Forest relating to ownership of assets and revenue recognition in the Impugned Disclosure Documents.

[60] Mr. Chan, Mr. Ip and Mr. Hung controlled the BVI Model, designed the actual documentation process and were aware this process was deceitful. Mr. Chan and Mr. Ip did not disclose that Sino-Forest's BVI subsidiaries could not obtain PRCs and thus could have no ownership claim to the BVI standing timber assets because those rights had never been registered. Mr. Chan and Mr. Ip knew the Villagers' Resolutions were never attached to purchase contracts. They knew the standing timber could not be identified using purchase contracts and their supporting documentation. Mr. Chan signed all sales contracts and therefore knew contracts were signed in the quarter after Sino-Forest recognized the revenue from them.

[61] Mr. Ip and Mr. Hung, by virtue of their control of the BVI Model, their design of the actual documentation process and their awareness this process was deceitful, knew the financial statement disclosure was misleading. Mr. Ip was in charge of all purchases of standing timber in the BVI Model and, as a senior officer of Sino-Forest, could have changed the process. Mr. Hung was a senior officer of Sino-Forest, was on the Disclosure Committee and had an extensive education in finance. He had influence over how information was disclosed. Both signed sub-certifications quarterly, verifying the misleading disclosure and did nothing to change it.

- [62] Mr. Ip and Mr. Hung permitted and acquiesced in the making of materially misleading statements by Sino-Forest relating to ownership of assets and revenue recognition in the Impugned Disclosure Documents.
- [63] Sino-Forest's disclosure during the Material Time misrepresented its ownership claims to its standing timber assets, based on Forestry Bureau Confirmations. These were not official documents, nor could they be relied upon in the event of a dispute of title in a court of law. Indeed, the forestry bureaus specifically stated the confirmations could only be used internally by Sino-Forest and may have exceeded the forestry bureau's authority to issue them, among other deficiencies. Despite this, Sino-Forest's AIFs made virtually identical disclosure during the Material Time regarding the Confirmations as proof of ownership of its BVI standing timber assets.
- [64] Mr. Chan and Mr. Ip knew Sino-Forest subsidiaries in the BVI Model could not obtain PRCs. Mr. Ip testified Sino-Forest never applied for PRCs in the BVI Model. The omission that Sino-Forest's BVIs could not obtain PRCs made the disclosure misleading.
- [65] Furthermore, Forestry Bureau Confirmations were only one of three attachments which were to accompany each BVI purchase contract; also noted as attachments were Villagers' Resolutions and Survey Reports. No Villagers' Resolutions were ever attached to a BVI purchase contract. The Impugned Disclosure Documents made no disclosure whatsoever that key attachments were missing from every BVI purchase contract, further weakening Sino-Forest's purported claim of ownership of the Standing Timber. These omissions were misleading.
- [66] The questionable authenticity of the Survey Reports, which also lacked any specific location descriptions, further weakened Sino-Forest's ownership claims. Neither the purchase contracts nor the Survey Reports provided sufficient information so that the standing timber assets could be independently located.
- [67] Sino-Forest failed to register its ownership of Standing Timber in the BVI Model and therefore did not become the legal owner, contrary to its disclosure. The Merits Panel found that this is critical information a reasonable investor would consider important in making an investment decision. The disclosure Sino-Forest did provide significantly understated this risk, since this lack of proof of ownership related to approximately 70% of Sino-Forest total timber holdings by hectare and on a value basis.
- [68] Sino-Forest failed to disclose in the Impugned Disclosure Documents the three fundamental flaws in the Standing Timber purchase contracts which relate to ownership of assets: backdating of contracts post-quarter end, insufficient proof of ownership, and failure to identify the specific assets being acquired.
- [69] With respect to revenue recognition, Sino-Forest's practice of creating and executing sales contracts in the quarters after revenue related to those transactions was recognized was contrary to the revenue recognition process set out in Sino-Forest's continuous disclosure documents.

## **2. Effects of the Four Frauds on Reported Revenue**

- [70] The Merits Panel found that a reasonable investor would have considered the overstatements in revenue, arising from the Four Frauds, described above, made

in the Impugned Disclosure Documents to be important when making an investment decision whether to buy, sell or hold Sino-Forest securities. These overstatements would also have cast doubt over the accuracy and integrity of all Sino-Forest financial statements, given the pervasiveness of the overstatements, which occurred over three years: 2008, 2009 and 2010. This undermining of trust in the accuracy and integrity of the statements would have a damaging effect on the market value of its securities, as trust is ultimately the foundation upon which our financial markets rest.

- [71] Sino-Forest's misleading disclosure about the Four Frauds was found to be undoubtedly important to a reasonable investor. Sino-Forest made statements in respect of revenue attributed to the Four Frauds that were in a material respect and at the time and in light of the circumstances under which they were made, misleading and untrue.
- [72] Mr. Chan authorized and permitted Sino-Forest's making of materially misleading statements about revenue attributed to three of the Four Frauds (the Gengma #1 Transactions, the Gengma #2 Transactions and the 450 Transactions). Overstatements of revenue resulting from these three frauds over an extended period were found to undermine trust in the accuracy and integrity of Sino-Forest's financial statements and to have a damaging effect on the market value of its securities.
- [73] Mr. Ip was found to have been directly and deeply involved in the Dacheng Transactions fraud from the very beginning. Mr. Ip had intimate knowledge of the Gengma #1 Transactions and the Gengma #2 Transactions. He was one of the key decision-makers in the extensive planning of the fraudulent transactions in the 450 Transactions. Mr. Ip permitted and acquiesced in Sino-Forest's making of materially misleading statements about revenue attributed to the Four Frauds.
- [74] Mr. Ho was found to have been directly involved in the 450 Transactions. In the Gengma #2 Transactions, Mr. Ho was aware of the circular flow of funds to settle the outstanding receivables. He participated in orchestrating the Dacheng Transactions fraud. Mr. Ho permitted and acquiesced in Sino-Forest's making of materially misleading statements about revenue attributed to three of the Four Frauds.

### **3. Statements Regarding Internal Controls**

- [75] The Merits Panel found that a reasonable investor would find Sino-Forest's failure to properly disclose the material weakness in its internal controls to be important when making a decision to buy, sell or hold Sino-Forest securities. Sino-Forest's disclosure was wholly inadequate and failed to reveal that the recording of purchases, sales and settlement of standing timber in the BVI Model was concentrated solely in Mr. Hung. Further, the scope of the BVI Model, which accounted for approximately 70% of Sino-Forest revenue between 2007 and 2010, was not disclosed. This effectively concealed the significance of this concentration of duties.
- [76] Mr. Chan could easily have remediated this weakness but chose not to do so, because it was integral to the Standing Timber Fraud. He knew the disclosure was wholly inadequate. Mr. Chan authorized and permitted the making of materially misleading statements by Sino-Forest regarding the material

weakness in its internal controls. His rationale for not disclosing this weakness was to perpetuate the Standing Timber Fraud.

- [77] While Mr. Hung cannot be held responsible for Mr. Chan's failure to remediate this weakness, he acquiesced in this failure. In addition, by virtue of his position on the Disclosure Committee, as a senior officer of Sino-Forest and his extensive education, Mr. Hung acquiesced in the making of materially misleading statements by Sino-Forest regarding the material weakness in its internal controls in its financial statements.

### **C. Greenheart**

- [78] The Merits Panel found that Mr. Chan was the beneficial owner of Fortune Universe and Montsford, which together owned 30% of Greenheart Resources, and received over US \$22 million in cash and securities in consideration for the Greenheart Transactions. Mr. Chan did not disclose his 30% interest through nominees in Greenheart, nor did he disclose his interest in the Second and Third Transactions to the Board of Directors or in Sino-Forest financial statements. In fact, Mr. Chan actively concealed his interests by hiding behind two nominee companies he organized in the names of friends and which were administered over the years by his executive assistant.
- [79] The omission of disclosure of Mr. Chan's interest is a dishonest act. Since investors were entitled to rely on Sino-Forest's public disclosure before risking their funds, the omission of disclosure of Mr. Chan's interest in Greenheart Resources and the Transactions created a risk to investors, who were unable to make informed decisions.
- [80] The Merits Panel found that Mr. Chan did not perpetrate this fraud on a whim. Mr. Chan was the beneficial owner of Fortune Universe and Montsford by at least 2005, a year before Sino-Forest made its initial investment. Through his long-time assistant he directed the establishment and organization of these companies. He chose their nominee owners and controlled the material decisions. Even the company seals were kept in his assistant's possession; these companies could not conduct important business without her approval. Mr. Chan carefully controlled the disposition of funds received from the Transactions, and the sales and use of proceeds of the Sino-Forest shares received from the Transactions. This fraud took years to plan and execute. The premeditation involved on the part of Mr. Chan is evident from the document trail created in execution of the fraud.
- [81] Mr. Chan did not disclose his interest in Greenheart Resources to the Board of Directors. In contrast, another director who had a 5% interest did disclose his interest and this interest was disclosed in the Impugned Disclosure Documents. Moreover, Mr. Chan actively hid his ownership by using nominee companies to further obscure his interest. By using Fortune Universe and Montsford, there is no doubt Mr. Chan was deliberate in his deceit and dishonesty.
- [82] Sino-Forest failed to disclose Mr. Chan's 30% interest in Greenheart Resources and the Second and Third Transactions in the Impugned Disclosure Documents. The Merits Panel found that these were facts a reasonable investor would consider important in making an investment decision with respect to Sino-Forest securities. The Merits Panel found that Mr. Chan, as Chairman and CEO,

authorized, permitted and acquiesced in Sino-Forest's making of materially misleading statements.

#### **D. Misleading Staff**

- [83] The Merits Panel found that Mr. Chan, Mr. Ip, Mr. Hung, Mr. Yeung and Mr. Ho misled Staff during interviews conducted as part of Staff's investigation. Mr. Chan unequivocally denied that Sino-Forest had control over Yuda Wood, despite at least three opportunities to tell the truth. Mr. Yeung misled Staff regarding his involvement in the creation and capitalization of Yuda Wood. Mr. Ho misled Staff regarding the control he had over Yuda Wood's bank accounts. Yuda Wood played a significant role in the Standing Timber Fraud. It was Sino-Forest's largest supplier in the BVI Model, at 20% of total BVI transaction value during the Material Time.
- [84] Mr. Ip and Mr. Hung misled Staff with respect to the Deceitful Documentation Process. Mr. Ip misled Staff with respect to Sino-Forest's role in the creation and issuance of Forestry Bureau Confirmations. Mr. Hung misled Staff with respect to the timing of payments made pursuant to the purchase contracts.

#### **IV. SANCTIONS**

- [85] Section 127 of the Act establishes the sanctions the Commission may impose, which include administrative penalties, disgorgement and various prohibitions. The respondents and Staff agree on the appropriate prohibitions to be ordered, but disagree on the appropriate administrative penalties and orders for disgorgement.
- [86] In determining the appropriate sanctions to be imposed, we are guided by the purposes of the Act, which include: protecting investors from unfair, improper or fraudulent practices and fostering fair and efficient capital markets and confidence in those markets.
- [87] The sanctions we impose must be preventative and protective, with a view to preventing likely future harm to Ontario's capital markets. They are not intended to be punitive.<sup>3</sup>
- [88] The Commission has considered a non-exhaustive list of factors in determining which sanctions are appropriate, including the following which were referred to by the parties in their submissions:
- a. the seriousness of the conduct;
  - b. the respondents' experience in the marketplace;
  - c. the level of the respondents' activity in the marketplace;
  - d. whether or not there has been a recognition by the respondents of the seriousness of the improprieties;
  - e. the size of any profit made or loss avoided from the illegal conduct;
  - f. the restraint any sanctions may have on the ability of the respondents to participate without check in the capital markets;

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<sup>3</sup> *Mithras Management Ltd (Re)* (1990), 13 OSCB 1600 at 1610-1611; *Committee for Equal Treatment of Asbestos Minority Shareholders v Ontario (Securities Commission)*, 2001 SCC 37, [2001] 2 SCR 132 at paras 42-43.

- g. the effect any sanction might have on the livelihood of the respondents;
- h. the shame or financial pain that any sanction would reasonably cause the respondents;
- i. the respondents' ability to pay any financial sanctions;
- j. the reputation and prestige of the respondents;
- k. whether or not the sanctions imposed may serve to deter not only those involved in the case being considered, but any like-minded people from engaging in similar abuses of the capital markets (specific and general deterrence); and
- l. mitigating factors, including the respondents' remorse.<sup>4</sup>

[89] With respect to specific and general deterrence, the Supreme Court of Canada has recognized that general deterrence is an "appropriate, and perhaps necessary, consideration in making orders that are both protective and preventative."<sup>5</sup> "The weight given to general deterrence will vary from case to case and is a matter within the discretion of the Commission."<sup>6</sup>

[90] The sanctions we impose must be proportionate to the circumstances and the conduct of each respondent. Given that the consequences of the respondents' misconduct contributed to the collapse of a multi-billion dollar public company, and are without precedent in Commission proceedings, the quantum of prior administrative penalties provide only a very limited basis for comparison.

#### **A. Administrative Penalties**

[91] Administrative penalties are intended to achieve both specific and general deterrence.<sup>7</sup> An administrative penalty may not achieve these objectives if it is outweighed by the benefit wrongdoers gain from non-compliance with the Act.<sup>8</sup> However, an undue emphasis on general deterrence may result in an administrative penalty that is disproportionate.<sup>9</sup>

[92] The Commission has imposed significant administrative penalties for fraudulent conduct, particularly where the conduct takes place over an extended period of time.<sup>10</sup>

[93] The Commission may impose an administrative penalty of up to \$1 million for each failure to comply with Ontario securities law.

[94] Staff seek the following administrative penalties:

- a. Mr. Chan – a total of \$5,000,000, being \$1,000,000 for each of the categories of conduct found by the Merits Panel – Standing Timber Fraud,

<sup>4</sup> *Belteco Holdings Inc (Re)* (1998), 21 OSCB 7743 at 7746; *MCJC Holdings Inc (Re)* (2002), 25 OSCB 1133 at 1135; *Sabourin (Re)*, 2010 ONSEC 10, 33 OSCB 5299 (**Sabourin**) at para 60.

<sup>5</sup> *Cartaway Resources Corp (Re)*, 2004 SCC 26, [2004] 1 SCR 672 (**Cartaway**) at para 60.

<sup>6</sup> *Cartaway* at para 64.

<sup>7</sup> *Limelight Entertainment Inc (Re)*, 2008 ONSEC 28, 31 OSCB 1727 (**Limelight**) at para 67.

<sup>8</sup> *Rowan (Re)*, 2009 ONSEC 46, 33 OSCB 91 at paras 73-74.

<sup>9</sup> *Cartaway* at para 64.

<sup>10</sup> See e.g. *Phillips (Re)*, 2015 ONSEC 36, 38 OSCB 9311 at paras 58 and 69; *Sextant Capital Management Inc (Re)*, 2012 ONSEC 17, 35 OSCB 5213 at paras 34-35; *Sabourin* at paras 76-86; *Al-Tar Energy Corp (Re)*, 2011 ONSEC 1, 34 OSCB 447 (**Al-Tar**) at paras 47-57.

standing timber misleading disclosure, Greenheart Transactions fraud, Greenheart Transactions misleading disclosure, and misleading Staff;

- b. Mr. Ip – a total of \$2,650,000, being \$1,000,000 for the Standing Timber Fraud, \$900,000 for standing timber misleading disclosure, and \$750,000 for misleading Staff;
- c. Mr. Hung – a total of \$2,250,000, being \$1,000,000 for the Standing Timber Fraud, \$750,000 for standing timber misleading disclosure, and \$500,000 for misleading Staff;
- d. Mr. Ho – a total of \$2,000,000, being \$1,000,000 for the Standing Timber Fraud, \$500,000 for standing timber misleading disclosure, and \$500,000 for misleading Staff; and
- e. Mr. Yeung – \$300,000 for misleading Staff.

[95] The respondents submit that lower total administrative penalties are appropriate, but do not allocate those administrative penalties among the categories of misconduct found by the Merits Panel. The respondents submit that the following administrative penalties are appropriate:

- a. Mr. Chan – \$1,750,000;
- b. Mr. Ip – \$500,000;
- c. Mr. Hung – \$500,000;
- d. Mr. Ho – \$500,000; and
- e. Mr. Yeung – no administrative penalty.

[96] There is common ground among Staff and the respondents that overall sanctions must be considered in respect of each respondent and they must be proportionate to the conduct and circumstances of each of them. Financial sanctions must also bear an appropriate relationship to other sanctions imposed by the Commission.

[97] In support of these administrative penalties, Staff emphasize the seriousness of the respondents' conduct, and the need for specific and general deterrence. In respect of Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho, Staff note the lengthy period of time over which their conduct occurred and their repeated breaches of the Act.

[98] The respondents submit that Staff are placing undue emphasis on general deterrence. They assert that amounts sought by Staff are not required for specific deterrence given the respondents' current circumstances.

[99] The respondents' conduct led to a market reaction resulting in a loss of approximately CA \$6 billion in equity market capitalization to investors. We need to take into account the enormity of the effects of the conduct of the respondents. In addition, it should be considered that we do not generally apply our penalties to each misstatement or instance of fraudulent conduct occurring even over an extended period of time, as here. If that approach were taken, the sanctions sought by Staff would be multiplied many times over since the misstatements and fraudulent acts occurred over years to the point where a CA \$6 billion market loss was precipitated, separate and apart from losses on outstanding debt. In light of that history, for key perpetrators in such a

downfall, a \$1 million dollar maximum administrative penalty is not disproportionate. There are no Commission proceedings involving consequences to investors based on overall financial losses as severe as in this case.

- [100] The Standing Timber Fraud was an elaborate scheme, executed over many years, to defraud investors. This fraud relates to the majority of the assets and revenue of Sino-Forest. Mr. Chan, Mr. Ip, Mr. Ho and Mr. Hung orchestrated a complex web of deceit with fictitious transactions and false documents. They misled investors about the ownership of standing timber, and how and when revenue was recognized. They concealed control and related party relationships with supposedly arms' length suppliers and customers. They misled the Board of Directors, auditors and investors. Each quarter they certified and sub-certified that Sino-Forest disclosure was true when they knew it was not. Over many years, they spun an intricate network of misstatements that resulted in the loss of CA \$6 billion in equity market capitalization, in addition to bond investor losses. They did so with full subjective knowledge; they knew their conduct was deceitful and put investors' pecuniary interests at risk. They engaged in repeated and ongoing deception.
- [101] As well, Mr. Chan fraudulently concealed his interest in Greenheart Resources from the Board and investors, and authorized and permitted Sino-Forest's misleading disclosure. It is serious misconduct for any officer; Mr. Chan was not only CEO but Chairman of the Board and was looked to as the 'visionary' for the enterprise.
- [102] Misleading Staff is a particularly offensive violation of the public interest. In order for the Commission to fulfill its mandate and ensure confidence in capital markets, those involved in the capital markets must provide full and accurate information to the Commission.<sup>11</sup>
- [103] The respondents submit that their misleading statements to Staff do not merit more than a nominal administrative penalty, because Staff's investigation was not obstructed by their conduct. We reject this submission. The Merits Panel found that the respondents misled Staff. We cannot speculate about the state of Staff's knowledge at the time the statements were made, and be more lenient if we think that Staff's investigations were not prolonged by the misleading statement. We rarely if ever have a line of sight into Staff's investigations to establish the impact a misstatement will have on Staff's inquiries or the establishment of the proof they will need to advance at a hearing.
- [104] We are cognizant of the fact that prohibitions on market participation, including director and officer bans, will have very little deterrent effect since the respondents reside outside of North America and are very unlikely to seek to participate here again or be accepted in the Canadian business community. Specific and general deterrence requires substantial financial penalties to deter those who would target Ontario capital markets from outside of our jurisdiction. If such bans will, in particular circumstances, provide little deterrence, we must use financial penalties to fill this need and the quantum can then be appropriately larger than in cases where other tools will provide such deterrence. In this case, the administrative penalties we have determined to impose are required given both the magnitude of the consequences that flowed from the

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<sup>11</sup> *Wilder v Ontario Securities Commission* (2001), 53 OR (3d) 159 (CA) at para 22.

respondents' misconduct as well as the more limited deterrent effect market prohibitions will have.

- [105] The respondents submit that the principle of totality should be applied so as to reduce the administrative penalties. They submit that, notwithstanding our system of penalties for overall misconduct, as opposed to multiple counts for each and every instance of non-compliance, separate sanctions should not be imposed for the frauds and the materially misleading statements relating to the frauds. This would further reduce the consequences for misconduct that led to a massive corporate failure and are inappropriate in these circumstances. Fraud and misleading disclosures are discrete violations in this case. It makes no sense that a corporate officer who controls aspects of the issuer's disclosure record should not be separately sanctioned for authorizing misleading statements to be disseminated into the market when he or she knows them to be false. Their actions or failure to act are at the final stage where investor harm can be mitigated and their determination to make materially misleading statements needs to be separately sanctioned and deterred. Each and every misstatement provided a separate opportunity for each of these respondents to have changed course and correct the misstatement, and in each case, they failed to do so.
- [106] The respondents submit that the principle of parity should limit the administrative penalties ordered, because these penalties should be proportionate to the conduct of each respondent in the circumstances, and to administrative penalties imposed in Commission decisions involving similar conduct. The respondents submit that the administrative penalties sought by Staff are unprecedented, and are significantly higher than those imposed by the Commission for similar conduct. In particular, the respondents note that the highest administrative penalty that has been imposed by the Commission for misleading Staff is \$250,000.
- [107] Among the respondents, we do need to be mindful of parity of treatment and have analyzed the role and circumstances of each Respondent in that light.
- [108] Staff submit that Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho had experience in the marketplace through their senior positions with Sino-Forest, and that their experience is an aggravating factor. In contrast, the respondents submit that they lacked training regarding Ontario securities law despite their senior positions. Their lack of training, they submit, should be a mitigating factor in determining sanctions.
- [109] Mr. Chan, as CEO and founder, made the decision to issue securities in Ontario; he cannot now rely on his lack of knowledge. Moreover, he was in the best position to mandate that sufficient training be offered to Sino-Forest employees, and he did not. His submission holds no merit. As for Mr. Ip, Mr. Hung and Mr. Ho, we accept that there was limited evidence of formal training; however, knowledge of Ontario securities law was not required to know that the actual purchase, sales and settlement processes differed dramatically from what was disclosed to the Board, the auditors and ultimately, to investors in the financial statements. The respondents simply had to tell the truth – and they did not.
- [110] The respondents submit that their inability to pay the amounts sought by Staff should be taken into account, and that this factor supports reduced administrative penalties. Mr. Ip, Mr. Hung and Mr. Yeung submit that they

supplied evidence that there is no likelihood they will be able to pay the administrative penalties sought by Staff. Mr. Ho submits that an inference should be drawn regarding his inability to pay given his compensation at Sino-Forest and the passage of time.

- [111] Ability to pay is an acknowledged sanctioning factor, but is not determinative. Its importance will vary from case to case and respondent to respondent. Mr. Chan did not provide evidence of his financial circumstances in that regard, so this factor was not considered in his case. For the others, we need to weigh the compelling need for general deterrence, among other factors, in relation to the remaining sanctioning factors, including ability to pay. Only with regard to Mr. Yeung did we find that his circumstances pointed to the appropriateness of a lower penalty on the grounds of inability to pay, bearing in mind his deteriorating health and the nature of his misconduct.
- [112] The respondents submit that they have expressed remorse in the circumstances. They do not feel responsible for investors' losses, but are concerned about what has happened to Sino-Forest and feel shame at being the subject of this proceeding. Staff submits that none of the respondents have expressed remorse, and any shame they have felt is a natural consequence of their conduct. We address the respondents' individual expressions of remorse or shame below.

### **1. Chan**

- [113] The Merits Panel made certain over-arching findings regarding the conduct of Mr. Chan, who was a co-founder of Sino-Forest in 1992 and Chairman of the Board and Chief Executive Officer during the Material Time until his resignation on August 28, 2011.
- [114] First, that Mr. Chan "was the driver steering Sino-Forest's business." In this role, his conduct did not meet the standard of a reasonably competent Chief Executive Officer acting in the circumstances at the time.
- [115] Second, Mr. Chan's role was not merely to be "working on the business" at a higher level of goal setting and strategy. The Merits Panel found that in addition to such a role, Mr. Chan "was in the business" and "he was also deeply involved in the day-to-day operations of Sino-Forest."
- [116] Third, the Panel found that it was not appropriate in assessing Mr. Chan's conduct to consider, as stated in the written submissions made on behalf of Mr. Chan in the Merits Hearing, the "significantly different business and cultural environment" particularly in the resource sector in China. Rather, the Merits Panel determined that:
- No matter what business Sino-Forest was engaged in, it was Chan's responsibility to ensure that Sino-Forest complied with Province of Ontario securities legislation as set out in the Ontario *Securities Act*.
- [117] Fourth, the Merits Panel considered Mr. Chan's submission that he lacked education regarding, and experience with, Ontario securities law, and found that did not diminish his obligation to comply with Ontario securities law.

- [118] Mr. Chan was the “ultimate and compensating control” over the transactions detailed in the Merits Decision. He was the ultimate “approver of all purchase contracts and the signatory on all sales contracts.”
- [119] Mr. Chan was responsible for oversight of the BVI Model and was the compensating control for the identified internal control weakness arising from a lack of segregation of duties in the recording of purchase and sale transactions and the settlement accounts in these transactions.
- [120] Three of the other respondents, all of whom were found to have engaged in fraud and other violations of Ontario securities law, reported directly to Mr. Chan.
- [121] The essence of the Standing Timber Fraud was the over-statement of assets and revenue resulting from the fraudulent scheme, which had three elements:
- a. undisclosed control of companies purportedly at arms’ length to Sino-Forest;
  - b. a Deceitful Documentation Process; and
  - c. internal control weaknesses or failures.
- [122] Staff proved Mr. Chan’s involvement in the fraudulent scheme in three distinct sets of transactions: (i) the 450 Transactions; (ii) the Gengma #1 Transactions; and (iii) the Gengma #2 Transactions.
- [123] The Merits Panel found that Mr. Chan knew that Sino-Forest controlled Yuda Wood, Sino-Forest’s largest supplier and hid this information from investors and others involved in the disclosure process.
- [124] The Panel also found that Mr. Chan, along with Mr. Ip and Mr. Hung, were the key architects of the Deceitful Documentation Process. For Mr. Chan this was not only involvement in the design and supervision of the deceit, but included his approval of all sales and purchase transactions in the BVI Model. He was the signatory on all sales contracts in this channel. He hid the actual, Deceitful Documentation Process from the Company’s board of directors, audit committee and auditors, placing investors at risk – a risk that materialized when these practices were called out by the Muddy Waters Report. Mr. Chan authorized payments before contracts were in place and instructed that plantation locations be kept secret, resulting in documentation that could not be properly used to verify transactions. He signed contracts after quarter ends in a manner inconsistent with the revenue recognition process disclosed in Sino-Forest’s financial statements. He failed to disclose the crucial fact that BVI entities could not be the legal owner of the timber resources under the law of China. In three of the four frauds, used as illustrations of the Standing Timber Fraud in the Merits Decision (the Gengma #1 Transactions, the Gengma #2 Transactions and the 450 Transactions), fictitious transactions were implemented with the effect of inflating Sino-Forest’s revenues with the knowledge and direction of Mr. Chan.
- [125] These fraudulent transactions resulted in materially misleading statements relating to the Company’s assets and revenues being used in prospectuses and continuous disclosure documents provided to the marketplace and the Commission. The Merits Panel made findings quantifying the effects of these misleading disclosures on the financial position of the Company in each of these frauds. The 450 Transactions inflated revenue by US \$30 million or 6.4% in the

fourth quarter of 2009. The Gengma #1 Transactions overstated the Company's revenue for 2010 by US \$231.3 million. The overstatement of revenues in the first and second quarters of 2010 was 29.3% and 51.6%, respectively. The Gengma #2 Transactions resulted in an overstatement between March 2008 and November 2009 of approximately US \$49.1 million.

- [126] Mr. Chan was responsible for the misleading disclosure of the Company's internal controls, deemed "wholly inadequate" by the Merits Panel, with regard to the concentration of duties with Mr. Hung in the BVI Model.
- [127] In the Greenheart Transactions, Mr. Chan engaged in fraud by concealing his interest in the transactions that resulted in control of Greenheart being acquired by Sino-Forest, and putting investors' pecuniary interests at risk.
- [128] Counsel for Mr. Chan argued that we should take into account that no financial loss was established as a result of this concealment and asked us to consider evidence offered in the Sanctions Hearing that the transactions were nonetheless at approximate fair value. The Merits Panel noted that Mr. Chan made extensive submissions on Greenheart's value, and found that it was not necessary for them to examine whether the price paid for Greenheart was reasonable or fair. For the reasons discussed below, we found Mr. Chan's evidence of fair value to be of virtually no probative value. In any event, it is pure speculation to say that the transaction may have been approved even if Mr. Chan's interest had been revealed.
- [129] Mr. Chan misled Staff about Sino-Forest's interest in Yuda Wood, completely denying the facts. These misleading statements are not excused or mitigated because Staff had other evidence of this concealed interest. It is an offence established by the misleading statement itself. This Panel will not consider speculation as to the extent to which this misleading statement may not have prolonged Staff's investigation where the misleading statement relates to a central aspect of the fraud perpetrated by the respondent.
- [130] There are no relevant mitigating factors. Mr. Chan's misconduct unquestionably involves among the most serious of harms to investors and confidence in the capital markets. The Standing Timber Fraud called into question ownership of assets valued at over US \$2.4 billion and revenue in excess of US \$3.3 billion. The Standing Timber Fraud was central to the events causing the demise of Sino-Forest, resulting in equity investor losses of approximately CA \$6 billion. The three sets of fraudulent transactions in which Mr. Chan was found to have had an operational role establish his involvement in the most serious of wrongdoing. This fraud was carried forward in misleading statements to investors in numerous Commission-mandated disclosure documents. The fraud was facilitated by an internal control weakness that he caused to occur and which was withheld from public scrutiny. His failure to disclose his interest in the Greenheart Transactions was consistent with his willingness to hide important facts from investors and to put his self-interest ahead of investors, either by perpetuating a fraud or receiving direct, tangible gains.
- [131] Mr. Chan had extensive experience in the forestry industry in China, as well as a business background that was sufficiently extensive that he could reasonably be expected to recognize that the Standing Timber Fraud involved extremely serious wrongdoing. He was the CEO and Chairman of a very large international

enterprise and a large capitalization TSX-listed company. He had the financial resources available to him to get advice based on a candid description of Sino-Forest's operations rather than misrepresentations and obfuscation of the truth.

- [132] Mr. Chan testified that he did nothing to cause Sino-Forest's demise but that it was caused by a series of actions not taken after he was relieved of his duties as CEO following the Muddy Waters Report. When asked what actions he would have taken instead, he replied he would have used the US \$1 billion cash available to buy back Sino-Forest stock in the market to demonstrate belief in the company.
- [133] In his Affidavit and evidence given at the Sanctions Hearing he did not recognize his own failings in his role as CEO and Chairman. Instead, he emphasized sadness and frustration at the events that occurred. Such a lack of acknowledgment is not an aggravating factor, and with multiple legal proceedings underway, he may well have had those proceedings in mind in framing his answers. We put no weight on this factor in this case.
- [134] Imposing the maximum available administrative penalties in this case is intended to deter others who might seek to target Ontario capital markets through fraudulent conduct and consequential violations of Ontario securities law. This will also deter Mr. Chan, although given the notoriety of this case, his personal loss of reputation is a powerful deterrent to him from re-entering our capital markets in any form.
- [135] Mr. Chan received high compensation, over CA \$22 million in cash compensation between 2007 and 2010, for his roles and benefited in that way, in addition to substantial sums from stock sales. Companies that Mr. Chan controlled also received over US \$22 million in cash and stock proceeds in connection with the Greenheart Transactions. He should not be rewarded because the fraud was detected and interrupted and he incurred losses on his Sino-Forest stock holdings, along with innocent public investors. Mr. Chan's assertions that there was no proof of loss to Sino-Forest in these transactions is not a factor that mitigates his receipt of substantial proceeds directly as a result of his deceit.
- [136] Mr. Chan did not provide evidence of his financial circumstances in an effort to mitigate sanctions.
- [137] We have determined that the following administrative penalties are appropriate:
- a. in respect of the Standing Timber Fraud, the maximum administrative penalty of \$1,000,000;
  - b. in connection with the materially misleading statements relating to the Standing Timber Fraud, the maximum administrative penalty of \$1,000,000;
  - c. in connection with the Greenheart Transactions fraud, the maximum administrative penalty of \$1,000,000;
  - d. in connection with the materially misleading statements relating to the Greenheart Transactions, the maximum administrative penalty of \$1,000,000; and
  - e. in connection with misleading Staff, the maximum administrative penalty of \$1,000,000.

[138] These administrative penalties total \$5 million.

## **2. Ip**

[139] With respect to Mr. Ip's conduct, the Merits Panel found that he

was intimately involved in virtually every aspect of the Standing Timber Fraud during the Material Time. He knowingly deceived Investors through his involvement in Sino-Forest's undisclosed control in companies with which it transacted and in the Deceitful Documentation Process.

[140] He was found to have had oversight of the execution of all four of the illustrative frauds. Mr. Ip led employees of the Sino-Panel Group of companies in the fraudulent recording of transactions in the Four Frauds that resulted in Sino-Forest's overstatement of assets and revenue during the Material Time.

[141] The Merits Panel found that Mr. Ip, by virtue of his control of critical aspects of the BVI Model, his participation in the design of the actual documentation process and his awareness that this process was deceitful, knew that Sino-Forest's financial statement disclosure was misleading. The Merits Panel found that Mr. Ip acquiesced in the making of materially misleading statements by Sino-Forest relating to ownership of assets and revenue recognition in Sino-Forest's misleading financial statements.

[142] Mr. Ip was found by the Merits Panel to have misled Staff about the Deceitful Documentation Process. When questioned about the preparation of Forestry Bureau Confirmations, he misled Staff by underplaying Sino-Forest's control over this process.

[143] Mr. Ip admits in his Affidavit submitted in the Sanctions Hearing to have received pre-tax compensation between 2008 and 2010 of over CA \$4 million.

[144] Staff seeks the maximum administrative penalty in respect of the Standing Timber Fraud of \$1 million, \$900,000 in respect of the misleading disclosure to investors and \$750,000 in respect of misleading Staff. The aggregate sought is \$2,650,000.

[145] We have determined that those amounts are appropriate.

[146] The Standing Timber Fraud could not have occurred but for his involvement in the Deceitful Documentation Process. The consequences, as with Mr. Chan, were catastrophic. This penalty is appropriate and necessary as a matter of general deterrence to those who would target Ontario capital markets for fraudulent conduct, whether from outside or inside of Canada. This is especially the case where director and officer and trading bans will have a limited impact on a person unlikely to have any future in Canadian business activities.

[147] It is Mr. Ip's evidence that he has been unemployed since his time at Sino-Forest, and that he currently has limited financial resources and assets. In light of the seriousness of Mr. Ip's conduct and the need to deter him and others from engaging in similar conduct, we do not place any weight on his evidence regarding his ability to pay monetary sanctions.

[148] Mr. Ip admits to shame concerning these proceedings, but no remorse for having personally perpetrated these frauds and misconduct. He "sincerely do(es) not believe that (he) is responsible." He feels "wronged" because he was simply

"following orders." He does not believe the CA \$6 billion loss was caused by his behavior and others in senior management, specifically Mr. Hung, Mr. Ho and Mr. Chan. Mr. Ip's expression of shame for what has befallen him is not an indication of remorse and will not act in mitigation of these sanctions.

### **3. Hung**

- [149] In connection with the Standing Timber Fraud, Mr. Hung had a central role in, and controlled, the Deceitful Documentation Process, which included directing the settlement of receivables and payables before the execution of contracts, and the preparation and backdating of purchase and sales documentation. He signed sub-certifications each financial quarter that there were no misstatements or omissions in Sino-Forest's disclosure, when he knew the disclosures were misleading and could not properly be relied upon by investors. Since 2005, Mr. Hung was a member of Sino-Forest's Disclosure Committee, but allowed these materially misleading disclosures to persist. He also acquiesced in Sino-Forest's making of materially misleading statements with regard to its internal controls.
- [150] Mr. Hung was found by the Merits Panel to have misled Staff with respect to the Deceitful Documentation Process, including the timing of payments made on the verbal instructions of Mr. Ip without seeing the relevant purchase contracts. His fraudulent conduct touched on the vast majority of Sino-Forest's assets and revenues.
- [151] Like Mr. Ip, Mr. Hung expressed shame at being subject to the Commission proceedings and the allegations, but not remorse for the consequences of his actions. These statements are not mitigating factors. While Mr. Hung feels shame for being a subject of these proceedings, when asked if he feels shame or remorse for the losses investors suffered, he replied: "No, I don't think I need to assume any responsibility there....there were different investors in Sino-Forest and the investors would make their investments according to their wishes." (November 20, 2017 at 56). He does not believe he did anything wrong other than being too trusting of others, namely the in-house accountants. As he did during the Hearing on the Merits, Mr. Hung continued the same finger-pointing at others and assumed no responsibility himself.
- [152] It is Mr. Hung's evidence that he has limited means and employment prospects. While we agree that he is unlikely to find himself employed in Canadian business endeavors in the future, the magnitude of the fraud and misconduct in which he participated requires a strong message of general deterrence. We do not place any weight on his evidence of his inability to pay monetary sanctions.
- [153] Mr. Hung received substantial cash compensation, totalling approximately CA \$1.2 million between 2007 and 2010, as well as gains from stock sales.
- [154] The seriousness of Mr. Hung's role in the Standing Timber Fraud, in light of his financial experience and knowledge, merits the highest penalty and we have determined that a \$1,000,000 administrative penalty is appropriate.
- [155] His actions led to the making of materially misleading disclosures, which were exacerbated by his membership on the Company's Disclosure Committee. For this conduct we have determined that an administrative penalty of \$750,000 is appropriate.

[156] Staff submit that we should impose an administrative penalty of \$500,000 on Mr. Hung for misleading staff. We have determined that \$250,000 is more appropriate, given that Mr. Hung admitted that the conduct that was the subject of the questions had occurred on more than one occasion and his lack of candor went only to the number of instances. With respect to Mr. Hung's responses to questions regarding his actions on Mr. Ip's instructions, his lack of candor is not as blatant as those of Mr. Chan and Mr. Ip.

[157] The aggregate amount of the administrative penalties we have determined are appropriate is therefore \$2,000,000.

#### **4. Ho**

[158] Mr. Ho, like Mr. Ip, was involved in the control Sino-Forest exercised over customers and suppliers, a central aspect of the Standing Timber Fraud. He exercised extensive financial control over Yuda Wood, its largest supplier. With his accounting background, he knew that this control and the resulting related party transactions called into question their legitimacy as reflected in Sino-Forest's disclosures. He provided sub-certifications that supported these misleading disclosures. He was a member of Sino-Forest's Disclosure Committee, but he allowed these misleading disclosures to continue uncorrected.

[159] Mr. Ho misled Staff regarding Sino-Forest's control of Yuda Wood. He was involved in three of the Four Frauds. The Merits Panel found that he had less involvement in the BVI Model than Mr. Chan, Mr. Ip and Mr. Hung.

[160] Mr. Ho received substantial cash compensation, totalling approximately CA \$1.2 million between 2007 and 2010, as well as gains from stock sales.

[161] The magnitude of the fraud, the need for general deterrence, and Mr. Ho's actions despite his accounting experience require the imposition of significant administrative penalties.

[162] We have determined that the administrative penalties of \$1,000,000 for the Standing Timber Fraud and \$500,000 for the materially misleading statements relating to the Standing Timber Fraud are appropriate. Mr. Ho's misstatements to Staff were clear and specific and deserve the proposed amount of \$500,000. The total of the administrative penalties we impose is \$2,000,000.

#### **5. Yeung**

[163] Mr. Yeung was not an officer of Sino-Forest. Unlike Mr. Hung and Mr. Ho, he was not responsible for the financial aspects of Sino-Forest's business and was not on the Disclosure Committee, and he had no financial background. He was, however, involved with Yuda Wood and Kun'an, two suppliers to Sino-Forest found by the Merits Panel to be related to Sino-Forest. The Merits Panel concluded that "it is not clear he knew Investors' economic interests were put at risk by his conduct."

[164] He was found to have misled Staff concerning his involvement in the capitalization of Yuda Wood.

[165] Mr. Yeung submits that his health should be taken into consideration as a mitigating factor. Staff submit that Mr. Yeung's health did not mitigate his conduct, but recognize that his health may be a factor we consider in assessing sanctions. By way of Affidavit, Mr. Yeung provided evidence that he has life-

threatening medical issues, which Staff do not contest. There is no reasonable probability that he will work again. He has very limited financial means.

[166] Staff seek an administrative penalty for misleading Staff in the amount of \$300,000. We agree that general deterrence requires a penalty in this case given the importance of Yuda Wood in the frauds that were perpetrated. However, due to Mr. Yeung's uncontested medical condition, we impose a nominal administrative penalty as an expression of general deterrence of \$1,000.

## **B. Disgorgement**

[167] The Commission may order a person or company who has not complied with Ontario securities law to disgorge to the Commission any amounts obtained as a result of the non-compliance. In *Limelight*, the Commission described its authority to order disgorgement as follows:

[P]aragraph 10 of subsection 127(1) of the Act provides that disgorgement can be ordered with respect to "any amounts obtained" as a result of non-compliance with the Act. Thus, the legal question is not whether a respondent "profited" from the illegal activity but whether the respondent "obtained amounts" as a result of that activity. In our view, this distinction is made in the Act to make clear that all money illegally obtained from investors can be ordered to be disgorged, not just the "profit" made as a result of the activity. This approach also avoids the Commission having to determine how "profit" should be calculated in any particular circumstance. Establishing how much a respondent obtained as a result of his or her misconduct is a much more straightforward test.<sup>12</sup>

[168] In *Phillips*, the Divisional Court noted that the wording of the disgorgement provision is broad; there is no limitation based on the individual's use of the funds obtained.<sup>13</sup>

[169] The Commission has considered the following factors, in addition to the general sanctioning factors, when contemplating a disgorgement order:

- a. whether an amount was obtained by a respondent as a result of non-compliance with the Act;
- b. the seriousness of the misconduct and the breaches of the Act and whether investors were seriously harmed;
- c. whether the amount that a respondent obtained as a result of non-compliance with the Act is reasonably ascertainable;
- d. whether the individuals who suffered losses are likely to be able to obtain redress; and
- e. the deterrent effect of a disgorgement order on the respondents and other market participants.<sup>14</sup>

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<sup>12</sup> *Limelight* at para 49.

<sup>13</sup> *Phillips v Ontario Securities Commission*, 2016 ONSC 7901 (Div Ct) (**Phillips**) at para 71.

<sup>14</sup> *Limelight* at para 52.

- [170] Staff seek disgorgement by Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho of the compensation they received from Sino-Forest between 2007 and 2010 in the form of salaries and bonuses.
- [171] Staff seek disgorgement by Mr. Chan of an additional \$38,181,282, which Staff submits is the total amount that Mr. Chan obtained through his conduct in respect of the Greenheart Transactions.
- [172] Staff do not seek disgorgement by Mr. Yeung.
- [173] Staff bear the onus of proving these amounts were obtained by the respondents "as a result of" their non-compliance with Ontario securities law.<sup>15</sup>
- [174] The respondents submit that no amounts should be disgorged by any of the respondents.

### **1. Greenheart Transactions**

- [175] Mr. Chan submits that no amounts should be disgorged in relation to Greenheart because no amount was obtained as a result of non-compliance with the Act. Mr. Chan's submissions rest principally on the approximate fair value opinion of Mr. Froese discussed below.
- [176] Mr. Chan submits that while the Merits Panel found that Mr. Chan failed to disclose his beneficial interests in Fortune Universe and Montsford, there is no evidence that this non-disclosure resulted in any amounts obtained by him as the term is used in the Act. Mr. Chan submits that in these circumstances "the amount obtained as a result of non-compliance" is the amount Sino-Forest paid above the value of the Greenheart shares. Mr. Chan submits there is no evidence that Sino-Forest paid above the value of the Greenheart securities and relies on Mr. Froese's approximate fair value analysis.
- [177] We dismiss Mr. Chan's submissions for two reasons.
- [178] First, we put little weight on Mr. Froese's opinion for the reasons discussed below.
- [179] Second, Mr. Chan's non-disclosure of his interest in Greenheart resulted in his beneficially owned companies, Fortune Universe and Montsford, realizing proceeds of CA \$38,181,282. Mr. Chan's personal endorsement of Greenheart to Sino-Forest's Board of Directors in 2007 undoubtedly had significant influence with the Board in approving the acquisition. But for Mr. Chan's presentation of this conflicted transaction without disclosing his personal interest in it, the opportunity would never have arisen, and Fortune Universe and Montsford would not have obtained the Sino-Forest shares at the time of the Second and Third Transactions in February 2009 and May 2010. It is incongruous to suggest Mr. Chan did not obtain these shares as a result of his non-disclosure of his interest in Greenheart, which put the pecuniary interests of investors at risk.
- [180] Mr. Chan submits that that the increase in share value he realized at the time of sale had nothing to do with the findings in the Merits Decision that he failed to disclose his interest in Greenheart. Mr. Chan submits that in *Blue Gold*,<sup>16</sup> the

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<sup>15</sup> *Limelight* at para 53.

<sup>16</sup> *Blue Gold Holdings Ltd (Re)*, 2016 ONSC 37, 39 OSCB 10177 (***Blue Gold***).

Commission held that disgorgement amounts should be calculated at the time of the breach without regard to any appreciation or diminution of value.

- [181] In *Blue Gold*, Staff did not seek disgorgement of shares which were remuneration for consulting services not related to the fraud. In contrast, with respect to Sino-Forest, the shares obtained, and the increase in share value, were directly related to Mr. Chan's non-disclosure and the Standing Timber Fraud, respectively. It was Mr. Chan, through his assistant, who instructed that the shares obtained by Fortune Universe and Montsford be sold in February and March 2011, after they had substantially increased in value. The appreciation in Sino-Forest's share price was directly related to the fraudulent profits Sino-Forest recorded in its misleading financial statements.
- [182] Mr. Chan also submits that there should be no disgorgement because the amounts sought by Staff are too remote so as to preclude them from having a sufficient causal connection to the breach.
- [183] We find no merit in this argument. Mr. Chan's entire course of conduct, which encompasses fraud, misleading statements and non-disclosure over a lengthy period of time, is directly related to Sino-Forest's share price appreciation, and therefore to the entire sale proceeds of Sino-Forest shares by Fortune Universe and Montsford.

**(a) Froese Evidence**

- [184] As discussed above, Mr. Chan submits investors suffered no losses as a result of his non-disclosure of his interest in Greenheart because Greenheart was acquired at approximate fair value. Again, we place little weight on the approximate fair value opinion. Sino-Forest's share price imploded just months after Mr. Chan, through his nominee companies, sold his shares to unsuspecting investors, who unquestionably suffered serious losses.
- [185] Mr. Chan submits that in determining appropriate sanctions and costs, the Panel must go beyond his non-disclosure and consider the entirety of the evidence. Mr. Chan's evidence is that the Greenheart Transactions were "a good deal." To support his claim, Mr. Chan introduced the expert opinion of Mr. Ken Froese who concluded that the Greenheart Transactions were at approximate fair value.
- [186] Mr. Froese testified that determining approximate fair value involves reviewing factors that are relevant in determining fair value and evaluating whether or not the transaction has occurred at or near that value. This is distinguished from fair value, which would involve an extensive process required in valuing a business, which Mr. Froese is not qualified to provide.
- [187] One factor in Mr. Froese's analysis was the Omnicorp/Greenheart share price (**094**) from January 2, 2009 to March 6, 2009 and March 1, 2010 to June 9, 2010. These two periods relate to the dates of the 2009 Transaction and the 2010 Transaction. However, the share price of 094 correlated closely with Sino-Forest's share price for a significant period of the Material Time. Indeed, following the release of the Muddy Waters Report, the 094 share price plunged, tracking the plunge in Sino-Forest's share price. Given that Sino-Forest's share price reflected the frauds described above, this factor is not useful in determining approximate fair value.

- [188] A second factor in Mr. Froese's analysis was whether independent directors opined on the transaction and/or the consideration paid. He failed to indicate in his report that it was the independent directors of Omnicorp, and not Sino-Forest, whose approval of the transaction assisted him in evaluating whether the transaction approximated fair value. There was no evidence that the Omnicorp directors were aware of Mr. Chan's fraudulent self-interest in the transaction. The Merits Panel has already found that the Sino-Forest directors were unaware of Mr. Chan's involvement because Mr. Chan failed to disclose it. There was no evidence regarding Omnicorp's process in evaluating the transaction, or the degree to which they relied on the share price ratio, which was affected by the Sino-Forest frauds. Therefore, this factor is not helpful in objectively determining approximate fair value.
- [189] A third factor was the consistency of the transaction with Sino-Forest's business strategy. While Mr. Froese was aware that Mr. Chan was regarded as the strategic 'visionary' involved in developing and implementing strategy, he did not consider how this influence weighed on the Board's decision to approve the acquisition. The link between Greenheart/Omnicorp and Sino-Forest business strategy is difficult to discern: Omnicorp was a failing Hong Kong electronics business prior to its acquisition of the Suriname forestry assets of Greenheart. Omnicorp was not in the forestry business prior to Mr. Chan's involvement (as a hidden owner of Greenheart) in the acquisition. This factor is not useful in determining approximate fair value.
- [190] Fourth, Mr. Froese relied on the 2007 Poyry valuation which valued Greenheart at no less than US \$200 million. However, the valuation itself relied on a transaction for wood logs sold to Sino-Forest at US \$175 per cubic meter; Mr. Chan himself signed this agreement on behalf of one of Sino-Forest's subsidiaries but the logs were never delivered to Sino-Forest. Mr. Froese agreed that these facts would make him question the reliability of the Poyry valuation and thus its usefulness in determining approximate fair value.
- [191] Finally, Mr. Froese testified that there is no professional standard to determine approximate fair value but that it was a "professional judgment call." He further testified that the range of approximate fair value was within plus or minus 20 to 25 percent, and that it was a "pretty rough, rough range."
- [192] Given the limitations on Mr. Froese's analysis, the Panel places little weight on his opinion that the Greenheart Transactions approximated fair value.
- [193] Moreover, it is not relevant whether or not Greenheart was "a good deal", as Mr. Chan insists. Mr. Chan's deliberate concealment of his interests in Greenheart, and his complex web of nominees, friends and family members involved in order to further obscure his interest, speaks volumes of his dishonesty, deceit and fraud. That is what is relevant in our determination of sanctions. He unquestionably received the proceeds in cash and shares through his nominee companies that Staff seeks to disgorge. This consideration came to him from a transaction in which he fraudulently concealed his interest, and should therefore be disgorged. Mr. Froese's evidence does not alter this conclusion.
- [194] Mr. Chan should not be permitted to benefit from his breach of Ontario securities law, which was premeditated and egregious. We agree with Staff's submissions that Mr. Chan should be required to disgorge CA \$38,181,282.

## 2. Salary and Bonuses

- [195] Staff seek the disgorgement by Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho of the compensation they received from Sino-Forest between 2007 and 2010 in the form of salaries and bonuses, in the following amounts:
- a. Mr. Chan – \$22,106,971;
  - b. Mr. Ip – \$1,859,710;
  - c. Mr. Hung – \$1,286,373; and
  - d. Mr. Ho – \$1,214,883.
- [196] The respondents submit that Staff has not established that these amounts were obtained as a result of the respondents' conduct. We disagree.
- [197] As a result of the respondents' conduct, approximately 70% of Sino-Forest's total timber holdings by hectare and approximately 70% of the revenue the company recognized between 2007 and 2010 cannot be verified. The Merits Panel found there was no evidence of the existence of the BVI assets that Sino-Forest valued at US \$2.9 billion on its 2010 financial statements. Following the Muddy Waters Report, Sino-Forest's equity market capitalization collapsed.
- [198] During the time that they caused Sino-Forest to record unverifiable assets and revenue, the respondents obtained compensation as officers of Sino-Forest. But for their conduct, they would not have received that compensation, as evidenced by the collapse of the company and the delisting of Sino-Forest's shares once their conduct was revealed.
- [199] The respondents submit that there is evidence of "real job duties" performed by them separate and apart from their misconduct, and the compensation for which Staff seeks disgorgement was in respect of those "real job duties" and not their misconduct. They point to the independence of the Compensation Committee and the public disclosure of the compensation criteria in support of this submission.
- [200] The respondents' submissions ignore that their misconduct resulted in the majority of Sino-Forest's revenue and assets being unverifiable, and contributed to investors losing billions of dollars. Neither those investors nor the Compensation Committee were aware of the respondents' misconduct.
- [201] The Commission may order full disgorgement of the amounts obtained regardless of how those funds were used.<sup>17</sup> The Commission has repeatedly ordered full disgorgement of the amounts obtained from investors.<sup>18</sup> Staff could have sought disgorgement of the amounts obtained from investors during the Material Time. Instead, Staff seeks disgorgement of the respondents' compensation.
- [202] The respondents rely on *Sabourin* in support of their submission that the Commission may not order disgorgement of salary. In *Sabourin*, the Commission did not order one of the respondents to disgorge his salary. The Commission may exercise its discretion not to order disgorgement of the full

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<sup>17</sup> *Phillips* at para 71.

<sup>18</sup> See e.g. *Phillips* at paras 79-80, *Limelight* at para 61, and *Al-Tar* at para 71.

amount. *Sabourin* is an example of the Commission doing so.<sup>19</sup> The Commission did not order the respondent Irwin to disgorge his salary because “[h]is role was primarily administrative and he appears to have acted only at the specific direction of Sabourin.”<sup>20</sup> In contrast, the Commission ordered the respondent Sabourin to make full disgorgement. *Sabourin* does not support the respondents’ submission that the Commission may not order disgorgement of salary. To the contrary, in respect of its conclusion regarding the respondent Irwin, the Commission stated “[i]n coming to that conclusion, we should not be taken to have concluded that a person paid a salary can never be held to have obtained... such amounts as a result of their non-compliance.”<sup>21</sup>

[203] The respondents obtained their salaries and bonuses during the Material Time as a result of their non-compliance with Ontario securities law. Therefore, they must disgorge their salaries and bonuses in the following amounts: Mr. Chan – \$22,106,971; Mr. Ip – \$1,859,710; Mr. Hung – \$1,286,373; and Mr. Ho – \$1,214,883.

### **C. Prohibitions on Market Participation**

[204] There was no disagreement between Staff and the respondents regarding the imposition of the participation bans. Although it is unlikely that any of the respondents will seek to enter the Canadian capital markets again, the public interest requires that this be put beyond the slightest doubt. For that reason, we impose the following non-financial sanctions on the respondents:

- a. an order that trading in any securities by each of them cease permanently;
- b. an order that the acquisition of any securities by each of them is prohibited permanently;
- c. an order that any exemptions contained in Ontario securities law do not apply to each of them permanently;
- d. an order that each of them be reprimanded;
- e. an order that each of them resign any positions that they hold as a director or officer of an issuer, registrant or investment fund manager;
- f. an order that each of them is prohibited from becoming or acting as a director or officer of any issuer, registrant or investment fund manager permanently; and
- g. an order that each of them be prohibited permanently from becoming or acting as a registrant, as an investment fund manager, or as a promoter.

### **V. COSTS**

[205] Section 127.1 of the Act authorizes the Commission to order a respondent to pay the costs of an investigation and the proceeding that follows it if the respondent has been found to have contravened Ontario securities law.

[206] Helpfully, Staff and the respondents made a joint submission regarding costs, which we find to be reasonable. We note that Staff has agreed not to seek costs

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<sup>19</sup> *Phillips (Re)*, 2015 ONSC 36, 38 OSCB 9311 at para 35.

<sup>20</sup> *Sabourin* at para 73.

<sup>21</sup> *Sabourin* at para 73.

from Mr. Yeung. Mr. Chan, Mr. Ip, Mr. Hung and Mr. Ho shall pay costs as follows:

- a. Mr. Chan shall pay \$2,038,704 of the costs of the investigation and hearing;
- b. Mr. Ip shall pay \$1,529,028 of the costs of the investigation and hearing, for which he shall be jointly and severally liable with Mr. Chan;
- c. Mr. Hung shall pay \$1,019,352 of the costs of the investigation and hearing, for which he shall be jointly and severally liable with Mr. Chan and Mr. Ip; and
- d. Mr. Ho shall pay \$509,676 of the costs of the investigation and hearing, for which he shall be jointly and severally liable with Mr. Chan, Mr. Ip and Mr. Hung.

## **VI. IMPACT OF OTHER JUDGMENTS**

[207] On March 14, 2018, the Superior Court of Justice in *Borelli, in his capacity as trustee of the SFC Litigation Trust v. Chan*, ordered Mr. Chan to pay US \$2,627,478,000 (**SFC Litigation Trust Order**). The conduct at issue in that proceeding overlaps to a significant degree with Mr. Chan's misconduct in this proceeding.

[208] A class action brought against Mr. Chan by Sino-Forest shareholders – *The Trustees of the Labourers' Pension Fund of Central and Eastern Canada et al v Sino-Forest Corp et al* – is pending in the Superior Court of Justice (**Shareholders Class Action**).

[209] To the extent that Mr. Chan makes payments in respect of SFC Litigation Trust Order or a final order in the Shareholders Class Action, these amounts should properly be credited against the disgorgement order we make against Mr. Chan. The Commission should not, in this type of case, compete with a broad class of harmed investors for amounts we have ordered to be disgorged. The respondents have urged us to suspend the ability to collect the disgorged amounts until these cases are reduced to absolutely final judgments. We disagree. Any litigation matter can take many turns and we do not wish to prevent Staff from exercising its judgment in how best to proceed in the coordination of these matters.

## **VII. CONCLUSION AND ORDER**

[210] With this sanctions decision, Commission proceedings involving these respondents are concluded. The duplicity demonstrated by these respondents in their actions resulting in the collapse of Sino-Forest is among the most serious misconduct engaged in by respondents in Commission proceedings, and especially by senior officers of a public company, including Mr. Chan, the purported 'visionary' who chose to betray the trust of the investors, employees and many other stakeholders of the company he led.

[211] These proceedings have been very protracted due to the complexity of the misconduct, the extent of evidence, the location of witnesses and many other factors. Nonetheless, this process has moved forward to this conclusion in a determined fashion, ensuring that these egregious facts and the sanctions that

have been imposed will not be lost on the respondents and others that seek to target Canadian capital markets.

[212] For all of these reasons, the following orders are in the public interest:

- a. Pursuant to paragraph 2 of subsection 127(1) of the Act, Mr. Chan, Mr. Ip, Mr. Hung, Mr. Ho and Mr. Yeung are permanently prohibited from trading in any securities;
- b. Pursuant to paragraph 2.1 of subsection 127(1) of the Act, Mr. Chan, Mr. Ip, Mr. Hung, Mr. Ho and Mr. Yeung are permanently prohibited from acquiring any securities;
- c. Pursuant to paragraph 3 of subsection 127(1) of the Act, all exemptions contained in Ontario securities law shall not apply to Mr. Chan, Mr. Ip, Mr. Hung, Mr. Ho and Mr. Yeung permanently;
- d. Pursuant to paragraphs 7, 8.1 and 8.3 of subsection 127(1) of the Act, Mr. Chan, Mr. Ip, Mr. Hung, Mr. Ho and Mr. Yeung shall resign from any positions they hold as a director or officer of any issuer, registrant or investment fund manager;
- e. Pursuant to paragraphs 8, 8.2 and 8.4 of subsection 127(1) of the Act, Mr. Chan, Mr. Ip, Mr. Hung, Mr. Ho and Mr. Yeung are permanently prohibited from becoming or acting as a director or officer of any issuer, registrant or investment fund manager;
- f. Pursuant to paragraph 8.5 of subsection 127(1) of the Act, Mr. Chan, Mr. Ip, Mr. Hung, Mr. Ho and Mr. Yeung are permanently prohibited from becoming or acting as a registrant, an investment fund manager or a promoter;
- g. Pursuant to paragraph 9 of subsection 127(1) of the Act:
  - i. Mr. Chan shall pay an administrative penalty of \$5,000,000;
  - ii. Mr. Ip shall pay an administrative penalty of \$2,650,000;
  - iii. Mr. Hung shall pay an administrative penalty of \$2,000,000;
  - iv. Mr. Ho shall pay an administrative penalty of \$2,000,000; and
  - v. Mr. Yeung shall pay an administrative penalty of \$1,000;
- h. Pursuant to paragraph 10 of subsection 127(1) of the Act:
  - i. Mr. Chan shall disgorge to the Commission \$60,288,253;
  - ii. Mr. Ip shall disgorge to the Commission \$1,859,710;
  - iii. Mr. Hung shall disgorge to the Commission \$1,286,373; and
  - iv. Mr. Ho shall disgorge to the Commission \$1,214,883;
- i. Each of the payments in paragraphs (g) and (h) is designated for allocation or use by the Commission in accordance with subclause 3.4(2)(b)(i) or (ii) of the Act;
- j. Pursuant to section 127.1 of the Act, the respondents shall pay costs to the Commission of \$5,096,760, as follows:

- i. Mr. Chan shall pay costs to the Commission of \$2,038,704;
  - ii. Mr. Ip. shall pay costs to the Commission of \$1,529,028, for which he shall be jointly and severally liable with Mr. Chan;
  - iii. Mr. Hung shall pay costs to the Commission of \$1,019,352, for which he shall be jointly and severally liable with Mr. Chan and Mr. Ip; and
  - iv. Mr. Ho shall pay costs to the Commission of \$509,676, for which he shall be jointly and severally liable with Mr. Chan, Mr. Ip and Mr. Hung; and
- k. Any payments made by Mr. Chan in respect of the SFC Litigation Trust Order or any final order in the Shareholders Class Action shall be credited against the disgorgement order against Mr. Chan in paragraph (h)(i).

Dated at Toronto this 9<sup>th</sup> day of July 2018

"D. Grant Vingoe"  
D. Grant Vingoe

"Deborah Leckman"  
Deborah Leckman

"Garnet W. Fenn"  
Garnet W. Fenn