

Criminal Litigation

Money-Laundering: Adverse Inference Drawn Following Defendant's Failure to Substantiate His Position

Introduction

As a sequel to our January newsletter on money laundering, this newsletter will discuss another recent judgment of the Court of Appeal, which relates to dealing with shares in a listed company.

Mr. Cheung Chun ("**Cheung**") was charged with one count of dealing in property known or believed to represent proceeds of indictable offence, in particular 10,991,000 shares in Hisense Kelon Electrical Holdings Company Limited. Cheung was tried in the District Court. He pleaded not guilty and chose not to give evidence. Cheung was acquitted after trial and the Secretary for Justice appealed to the Court of Appeal by way of case stated pursuant to section 84 of the District Court Ordinance (Cap 336). The appeal was allowed, whereby the Court of Appeal reversed the verdict and directed the trial be resumed¹. The District Court followed the decisions of the Court of Appeal and Cheung was convicted and sentenced to 5 years and 9 months imprisonment. Cheung made an application for leave to appeal against the conviction and sentence².

Background

Gu Chujun ("**Gu**") was the major shareholder and the Chairman of the Board of Directors of Greencool Technology Holdings Limited ("**Greencool**"). In 2002, Gu caused Greencool to acquire over 20% shareholdings in Guangdong Kelon Electrical Holdings Company Limited ("**Guangdong Kelon**"). Gu thereby became the single largest shareholder and the Chairman of the Board of Directors of Guangdong Kelon. Three BVI companies (collectively, the "**BVI Companies**") were subsequently set up:

1. BPH Ltd, with Mr. Xia Juxing ("**Xia**"), an employee of Greencool as one of the shareholder and director;
2. V&W Incorporation, with Mr. Li Xiangrong ("**Li**"), Gu's driver as the sole shareholder and director;
3. B&H Ltd, with Mr. Zhang Bomin ("**Zhang**"), an employee of Guangdong Kelon as the sole shareholder and director.

¹ Secretary of Justice v Cheung Chun, CACC 40/2013

² HKSAR v Cheung Chun, CACC 74/2014

Between 2002 and 2005, a total of 75,695,000 shares in Guangdong Kelon were transferred to the corporate securities accounts of the BVI Companies. In early 2005, Gu and other related persons were investigated by the Securities and Futures Commission of Hong Kong and China Securities Regulatory Commission. The trading of shares in Guangdong Kelon was suspended on 16 June 2005 (the “**Suspension**”) and Gu was arrested in July 2005.

In June 2007, Guangdong Kelon changed its company name to Hisense Kelon Electrical Holdings Company Limited (“**Hisense**”).

The Prosecution’s case

During January 2001 to July 2008, Cheung was employed by Greencool as Gu’s chauffeur, with a monthly salary of around HK\$15,000. Between 18th September 2007 and 18th April 2008, the BVI Companies transferred a total of 10,991,000 shares in Hisense (“**Shares**”) to Cheung’s personal security trading accounts, at a price of HK\$0.89 per share. Cheung subsequently sold 5,410,000 Shares to six Mainland residents at the same price of HK\$0.89 per share. These share transfers were conducted during the Suspension.

As the trading of Shares in the Hong Kong Stock Exchange resumed in January 2009, Cheung further sold 2,491,000 Shares at prices ranging from HK\$0.82 to HK\$4 per share. The remaining 3,100,000 Shares held in Cheung’s securities accounts were frozen due to the criminal prosecution.

It was the prosecution’s case that Cheung had reasonable grounds to believe that all or part of the 10,991,000 Shares he received from the BVI Companies represented proceeds of an indictable offence. The prosecution’s case based on, inter alia, the following:

1. Cheung must have known that Gu’s arrest was related to the financial problems of Hisense, and he must have known the reasons for the Suspension;
2. Cheung must have known the background of Zhang and Li. They have dealt with large volume of Shares during the Suspension and the circumstances were suspicious;
3. Cheung’s monthly salary was around HK\$15,000, he should not have financial resources to purchase Shares that were worth around HK\$10 million. Further, it appears that the transactions were not supported by corresponding money transfer;
4. Cheung purchased the Shares at a price of HK\$0.89 per Share and subsequently transferred part of the Shares to six Mainland residents at the same price.

The Defendant’s case

According to the 2007 Annual Report of Hisense, the value of each Share was negative RMB0.6348. In the circumstances, the Defendant alleged that at the material time, the

Shares did not constitute “property” under the Organized and Serious Crimes Ordinance (Cap 455) (“OSCO”). The Defendant’s second ground of appeal was that the Court had drawn adverse inference against the Defendant by reason of his dealing with the Shares, his relationship with Xia, Li and Zhang and his failure to produce supporting documents in the transfer of Shares. The Defendant argued that such adverse inference was inappropriate. There was no evidence to show that Gu has provided illegitimate funding to the BVI Companies or that the Defendant was aware of the BVI Companies’ source of funding. Further, the Shares may not be priced at HK\$0.89 per shares, the finding that the Defendant lacked financial resources to purchase the Shares was unsafe.

The Court of Appeal’s Reasoning

According to section 2 of the OSCO, property includes both movable and immovable property within the meaning of section 3 of the Interpretation and General Clauses Ordinance (Cap 1), which provides that property includes money, goods, choses in action and land, etc.

In respect of whether the Shares constitute property, the Court considered that the value of a listed company includes intangible assets such as customer relationship, goodwill and business methodologies. The Court rejected the Defendant’s allegation that the Shares did not fall within the meaning of Property by reason of its negative value. The Court considered that despite the value of the Shares, Hisense would still be liable to repay its debts. In this regard, the Shares must be a chose in action and therefore property under the OSCO.

In respect of the 2nd ground of appeal, it is well established that it was unnecessary for the prosecution to prove that the properties were, as a matter of fact, the proceeds of an indictable offence, because the conduct element of the offence is dealing with property. According to the case of *HKSAR v Pang Hung Fai*³, the Court shall consider whether right-thinking member of the community would have reasonable grounds to believe that the money in question represented proceeds of an indictable offence. Further, the Court shall also consider the Defendant’s knowledge and whether he would have reasonable grounds to believe that the money in question represented proceeds of an indictable offence.

Considering the overall circumstances of the prosecution’s case, the purchase of a large volume of Shares at HK\$0.89 per share was not a reasonable transaction. It further defied any commercial sense for the Defendant to sell half of the Shares he just purchased at the same price. The Defendant failed to offer explanation or produce any documentation to rebut the prosecution’s case. Therefore, the available evidence was sufficient for the Court to draw a necessary and irresistible inference that when the Defendant was dealing with the

³ HKSAR v Pang Hung Fai, Final Appeal (Criminal) No 8 of 2013

Shares, the Defendant knew or has reasonable ground to believe that the Shares represented proceeds of an indictable offence. The leave to appeal against conviction was therefore dismissed.

Conclusion

Despite the Defendant's attempt to argue that there might be other possible inferences to be drawn from the Shares transactions, in the absence of evidence, the Court of Appeal rejected the Defendant's argument. As this case demonstrates, adverse inference against a defendant can be difficult to rebut and merely denying the prosecution's case without proper substantiation may not be sufficient.

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Important: The law and procedure on this subject are very specialised and complicated. This article is just a very general outline for reference and cannot be relied upon as legal advice in any individual case. If any advice or assistance is needed, please contact our solicitors.

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