

## SFC Obtains Disqualification and Court Orders Against Hanergy's Former Chairman and Current Directors

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***The Court of First Instance's decision has important implications for directors of listed companies when failing to act in the best interests of the company.***

### Background

On July 15, 2015, the Securities and Futures Commission (SFC) suspended trading in shares of Hanergy Thin Film Power Group Limited (Hanergy), a company listed on the Main Board of The Stock Exchange of Hong Kong Limited. The SFC's action followed its investigation into a series of very substantial connected transactions between Hanergy and its parent company, Hanergy Holding Group Limited (Hanergy Holding). Hanergy's main source of revenue had come from selling solar-panel production systems to Hanergy Holding and Hanergy Holding's affiliates. The SFC alleged that Hanergy's former chairman, Mr. Li Hejun (Mr. Li), and four current independent non-executive directors, Ms. Zhao Lan (Ms. Zhao), Mr. Wang Tongbo, Mr. Xu Zheng (Mr. Xu), and Mr. Wang Wenjing, had failed to:

- Question the viability of Hanergy's business model
- Properly assess the financial position of the connected parties and hence the recoverability of the receivables they owed as a result of the relevant connected transactions
- Take proper steps to recover these receivables by putting the interests of the connected parties before that of Hanergy, and therefore did not act in Hanergy's best interest

The SFC commenced legal proceedings in the Court of First Instance on January 23, 2017 to seek disqualification orders against the former chairman and four current independent non-executive directors of Hanergy. In addition, the SFC sought a court order requiring Mr. Li to procure payment of all outstanding receivables that Hanergy Holding and its affiliates owed to Hanergy under various sales contracts, as well as to execute a guarantee securing their payment.

The SFC's approach in this case is consistent with its focus on holding individual wrongdoers accountable for their misconduct through the "vigorous exercise" of its broad powers under the Securities and Futures Ordinance, as previously stated by the SFC's head of enforcement, Thomas Atkinson.

## Decision

The court found that Mr. Li's breaches of duties were of a very serious nature given:

- His position as the chairman and executive director of Hanergy and the ultimate controller of both Hanergy and Hanergy Holding, which created a patent and serious conflict of interests
- The very substantial amount of money involved
- The period of time during which the breaches of duties took place

The court held that Mr. Li's breaches were not the result of incompetence or negligence, as he had a clear conflict of interests and plainly preferred the interests of Hanergy Holding and its affiliates to those of Hanergy. In addition, the court found that he had failed to exercise reasonable care and diligence in connection with an undisclosed loan of RMB900 million that a Mainland subsidiary of Hanergy had provided to Hanergy Holding in March 2014. Hanergy had failed to disclose this loan to its shareholders and had failed to seek independent shareholders' approval in accordance with the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

Based on these findings, the court disqualified Mr. Li from serving as a director or otherwise being involved in the management of any listed or unlisted corporation in Hong Kong for eight years. The court also ordered Mr. Li to procure Hanergy Holding and/or its affiliates to pay all outstanding receivables due to Hanergy under various sales contracts. Because Mr. Li had already executed a deed of guarantee in favor of Hanergy in respect of the amount owed by Hanergy Holding and/or its affiliates, and because Hanergy Option Limited (a company wholly owned by Mr. Li) had also executed a share charge in favor of Hanergy to secure Mr. Li's obligations under the deed of guarantee, the SFC no longer sought a court order requiring Mr. Li to execute a deed of guarantee.

In addition, the court found that Ms. Zhao, Mr. Wang Tongbo, Mr. Xu, and Mr. Wang Wenjing had been incompetent and, furthermore, had exhibited a marked indifference to their responsibilities as directors, particularly given that they had failed to:

- Make appropriate disclosures about the viability of Hanergy's business model, which a reasonable director should have questioned
- Properly assess the financial positions of the connected parties and hence the recoverability of the receivables due from them as a result of these connected transactions
- Take proper steps to recover these receivables, and therefore, did not act in Hanergy's best interest

The court ordered that Ms. Zhao and Mr. Wang Tongbo be disqualified for four years, and that Mr. Xu and Mr. Wang Wenjing be disqualified for three years (taking into account the longer period of default by Ms. Zhao and Mr. Wang Tongbo).

## Resumption of Trading

Hanergy has indicated its intention to seek a resumption of trading in its shares. As a first step, Hanergy will need to submit a disclosure document to the SFC for consideration. The disclosure document will need to address the SFC's concerns by providing detailed information on the company and its activities, business, assets, liabilities, financial performance, and prospects.

## Conclusion

The Court of First Instance's decision should remind directors of listed companies (including non-executive and independent non-executive directors) to always prioritize the interests of the listed company and its shareholders. This is particularly important when a listed company enters into connected transactions that may present a conflict of interests. Corporate misconduct is one of the SFC's key areas of focus and it will continue to take appropriate actions to hold listed company directors individually accountable for wrongdoing. Directors who fail to act in a listed company's best interests may be subject to an SFC investigation, as well as orders including — but not limited to — disqualification and compensation, pursuant to section 214 of the Securities and Futures Ordinance.

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