

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

**B E T W E E N :**

**THE TRUSTEES OF THE LABOURERS' PENSION FUND  
OF CENTRAL AND EASTERN CANADA and THE TRUSTEES OF THE INTERNATIONAL  
UNION OF OPERATING ENGINEERS LOCAL 793 PENSION PLAN FOR OPERATING  
ENGINEERS IN ONTARIO**

**Plaintiffs**

**- and -**

**SINO-FOREST CORPORATION, ERNST & YOUNG LLP, ALLEN T.Y. CHAN, W.  
JUDSON MARTIN, KAI KIT POON, DAVID J. HORSLEY, WILLIAM E. ARDELL, JAMES  
P. BOWLAND, JAMES M.E. HYDE, EDMUND MAK,  
SIMON MURRAY, PETER WANG, GARRY J. WEST,  
PÖYRY (BEIJING) CONSULTING COMPANY LIMITED, CREDIT SUISSE SECURITIES  
(CANADA), INC., TD SECURITIES INC., DUNDEE SECURITIES CORPORATION, RBC  
DOMINION SECURITIES INC., SCOTIA CAPITAL INC., CIBC WORLD MARKETS INC.,  
MERRILL LYNCH CANADA INC., CANACCORD FINANCIAL LTD. and MAISON  
PLACEMENTS CANADA INC.**

**Defendants**

*Proceeding under the Class Proceedings Act, 1992*

**STATEMENT OF CLAIM**

**(NOTICE OF ACTION ISSUED JULY 20, 2011)**

**TO: Sino-Forest Corporation**  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: David Horsley**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: Allen Chan**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: William Ardell**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: James Bowland**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: James Hyde**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: Edmund Mak**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: W. Judson Martin**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

**AND TO: Simon Murray**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3

- AND TO: Kai Kit Poon**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3
- AND TO: Peter Wang**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3
- AND TO: Garry West**  
Sino-Forest Corporation  
1208-90 Burnhamthorpe Rd W  
Mississauga, ON L5B 3C3
- AND TO: Ernst & Young LLP**  
222 Bay Street  
Toronto, ON M5K 1J7
- AND TO: Pöyry (Beijing) Consulting Company Limited**  
2208-2210 Cloud 9 Plaza  
No. 1118 West Yan'an Road  
Shanghai 200052  
PR CHINA
- AND TO: Credit Suisse Securities (Canada), Inc.**  
1 First Canadian Place  
100 King Street West, Suite 2900  
Toronto, Ontario M5X 1C9
- AND TO: TD Securities Inc.**  
66 Wellington Street West  
P.O. Box 1, TD Bank Tower  
Toronto, Ontario M5K 1A2
- AND TO: Dundee Securities Corporation**  
1 Adelaide Street East  
Toronto, ON M5C 2V9
- AND TO: RBC Dominion Securities Inc.**  
155 Wellington Street West, 17<sup>th</sup> Floor  
Toronto, Ontario M5V 3K7

- AND TO: Scotia Capital Inc.**  
40 King Street West, Scotia Plaza  
P.O. Box 4085, Station A  
Toronto, Ontario M5W 2X6
- AND TO: CIBC World Markets Inc.**  
161 Bay Street, Brookfield Place  
P.O. Box 500  
Toronto, Ontario M5J 2S8
- AND TO: Merrill Lynch Canada Inc.**  
BCE Place, Wellington Tower  
181 Bay Street, 4<sup>th</sup> and 5<sup>th</sup> Floors  
Toronto, Ontario M5J 2V8
- AND TO: Canaccord Financial Ltd.**  
161 Bay Street, Suite 2900  
P.O. Box 516  
Toronto, Ontario M5J 2S1
- AND TO: Maison Placements Canada Inc.**  
130 Adelaide Street West, Suite 906  
Toronto, Ontario M5H 3P5

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**DEFINED TERMS**

1. In this Statement of Claim, in addition to the terms that are defined elsewhere herein, the following terms have the following meanings:
  - (a) “**AI**” means Authorized Intermediary;
  - (b) “**AIF**” means Annual Information Form;
  - (c) “**Ardell**” means the defendant William E. Ardell;
  - (d) “**Bowland**” means the defendant James P. Bowland;
  - (e) “**Canaccord**” means the defendant Canaccord Financial Ltd.;
  - (f) “**CBCA**” means the *Canada Business Corporations Act*, RSC 1985, c. C-44, as amended;
  - (g) “**Chan**” means the defendant Allen T.Y. Chan also known as “Tak Yuen Chan”;
  - (h) “**CIBC**” means the defendant CIBC World Markets Inc.;
  - (i) “**CJA**” means the Ontario *Courts of Justice Act*, RSO 1990, c C-43, as amended;
  - (j) “**Class**” and “**Class Members**” means all persons and entities wherever they may reside who acquired securities of **Sino** during the **Class Period** either by primary distribution in Canada or an acquisition on the **TSX** or other secondary market in Canada, other than the **Defendants**, their past and present subsidiaries, affiliates, officers, directors, senior employees, partners, legal representatives, heirs, predecessors, successors and assigns, and any individual who is an immediate member of the family of an **Individual Defendant**;
  - (k) “**Class Period**” means the period from and including March 19, 2007 to and including June 2, 2011;
  - (l) “**Code**” means **Sino**’s Code of Business Conduct;

- (m) “**CPA**” means the Ontario *Class Proceedings Act, 1992*, SO 1992, c 6, as amended;
- (n) “**Credit Suisse**” means the defendant Credit Suisse Securities (Canada), Inc.;
- (o) “**Defendants**” means **Sino**, the **Individual Defendants**, **Pöyry**, **E&Y** and the **Underwriters**;
- (p) “**December 2009 Prospectus**” means **Sino**’s Final Short Form Prospectus, dated December 10, 2009, which **Sino** filed on **SEDAR** on December 11, 2009;
- (q) “**Dundee**” means the defendant Dundee Securities Corporation;
- (r) “**E&Y**” means the defendant, Ernst and Young LLP;
- (s) “**GAAP**” means Canadian generally accepted accounting principles;
- (t) “**Globe**” means *The Globe and Mail*;
- (u) “**Horsley**” means the defendant David J. Horsley;
- (v) “**Hyde**” means the defendant James M.E. Hyde;
- (w) “**Impugned Documents**” means the 2006 Annual Consolidated Financial Statements (filed on **SEDAR** on March 19, 2007), 2006 **AIF** (filed on **SEDAR** on March 30, 2007), 2006 Annual **MD&A** (filed on **SEDAR** on March 19, 2007), Management Information Circular dated April 27, 2007 (filed on **SEDAR** on May 4, 2007), Q1 2007 **MD&A** (filed on **SEDAR** on May 14, 2007), Q1 2007 Financial Statements (filed on **SEDAR** on May 14, 2007), **June 2007 Prospectus**, Q2 2007 **MD&A** (filed on **SEDAR** on August 13, 2007), Q2 2007 Financial Statements (filed on **SEDAR** on August 13, 2007), Q3 2007 **MD&A** (filed on **SEDAR** on November 12, 2007), Q3 2007 Financial Statements (filed on **SEDAR** on November 12, 2007), 2007 Annual Consolidated Financial Statements (filed on **SEDAR** on March 18, 2008), 2007 **AIF** (filed on **SEDAR** on March 28, 2008), 2007 Annual **MD&A** (filed on **SEDAR** on March 18, 2008),



Amended 2007 Annual **MD&A** (filed on **SEDAR** on March 28, 2008), Management Information Circular dated April 28, 2008 (filed on **SEDAR** on May 6, 2008), Q1 2008 **MD&A** (filed on **SEDAR** on May 13, 2008), Q1 2008 Financial Statements (filed on **SEDAR** on May 13, 2008), Q2 2008 **MD&A** (filed on **SEDAR** on August 12, 2008), Q2 2008 Financial Statements (filed on **SEDAR** on August 12, 2008), Q3 2008 **MD&A** (filed on **SEDAR** on November 13, 2008), Q3 2008 Financial Statements (filed on **SEDAR** on November 13, 2008), 2008 Annual Consolidated Financial Statements (filed on **SEDAR** on March 31, 2009), 2008 Annual **MD&A** (filed on **SEDAR** on March 16, 2009), Amended 2008 Annual **MD&A** (filed on **SEDAR** on March 17, 2009), 2008 **AIF** (filed on **SEDAR** on March 31, 2009), Management Information Circular dated April 28, 2009 (filed on **SEDAR** on May 4, 2009), Q1 2009 **MD&A** (filed on **SEDAR** on May 11, 2009), Q1 2009 Financial Statements (filed on **SEDAR** on May 11, 2009), **June 2009 Prospectus**, Q2 2009 **MD&A** (filed on **SEDAR** on August 10, 2009), Q2 2009 Financial Statements (filed on **SEDAR** on August 10, 2009), Q3 2009 **MD&A** (filed on **SEDAR** on November 12, 2009), Q3 2009 Financial Statements (filed on **SEDAR** on November 12, 2009), **December 2009 Prospectus**, 2009 Annual **MD&A** (filed on **SEDAR** on March 16, 2010), 2009 Audited Annual Financial Statements (filed on **SEDAR** on March 16, 2010), 2009 **AIF** (filed on **SEDAR** on March 31, 2010), Management Information Circular dated May 4, 2010 (filed on **SEDAR** on May 11, 2010), Q1 2010 **MD&A** (filed on **SEDAR** on May 12, 2010), Q1 2010 Financial Statements (filed on **SEDAR** on May 12, 2010), Q2 2010 **MD&A** (filed on **SEDAR** on August 10, 2010), Q2 2010 Financial Statements (filed on **SEDAR** on August 10, 2010), Q3 2010 **MD&A** (filed on **SEDAR** on November 20, 2010), Q3 2010 Financial Statements (filed on **SEDAR** on November 20, 2010), 2010 Annual **MD&A** (March 15, 2011), 2010 Annual Audited Financial Statements (filed on **SEDAR** on March 15, 2011), 2010 **AIF** (filed on **SEDAR** on March 31, 2011) and Management Information Circular dated May 2, 2011 (filed on **SEDAR** on May 10, 2011);

- (x) “**Individual Defendants**” means **Chan, Martin, Poon, Horsley, Ardell, Bowland, Hyde, Mak, Murray, Wang, and West**, collectively;
- (y) “**June 2007 Prospectus**” means **Sino**’s Short Form Prospectus, dated June 5, 2007, which **Sino** filed on **SEDAR** on June 5, 2007;
- (z) “**June 2009 Prospectus**” means **Sino**’s Final Short Form Prospectus, dated June 1, 2009, which **Sino** filed on **SEDAR** on June 1, 2009;
- (aa) “**Maison**” means the defendant Maison Placements Canada Inc.
- (bb) “**Martin**” means the defendant W. Judson Martin;
- (cc) “**Mak**” means the defendant Edmund Mak;
- (dd) “**MD&A**” means Management’s Discussion and Analysis;
- (ee) “**Merrill**” means the defendant Merrill Lynch Canada Inc.;
- (ff) “**Muddy Waters**” means Muddy Waters LLC;
- (gg) “**Murray**” means the defendant Simon Murray;
- (hh) “**OSA**” means the *Securities Act*, RSO 1990 c S.5, as amended;
- (ii) “**OSC**” means the Ontario Securities Commission;
- (jj) “**Plaintiffs**” means the plaintiffs, the Trustees of the Labourers’ Pension Fund of Central and Eastern Canada (“**Labourers**”) and the Trustees of the International Union of Operating Engineers Local 793 Pension Plan for Operating Engineers in Ontario (“**Operating Engineers**”), collectively;
- (kk) “**Poon**” means the defendant Kai Kit Poon;
- (ll) “**Pöyry**” means the defendant, Pöyry (Beijing) Consulting Company Limited;
- (mm) “**PRC**” means the People’s Republic of China;

- (nn) “**Representation**” means the statement that Sino’s financial statements complied with **GAAP**;
- (oo) “**RBC**” means the defendant RBC Dominion Securities Inc.;
- (pp) “**Scotia**” means the defendant Scotia Capital Inc.;
- (qq) “**SEDAR**” means the system for electronic document analysis and retrieval of the Canadian Securities Administrators;
- (rr) “**Securities Legislation**” means, collectively, the *OSA*, the *Securities Act*, RSA 2000, c S-4, as amended; the *Securities Act*, RSBC 1996, c 418, as amended; the *Securities Act*, CCSM c S50, as amended; the *Securities Act*, SNB 2004, c S-5.5, as amended; the *Securities Act*, RSNL 1990, c S-13, as amended; the *Securities Act*, SNWT 2008, c 10, as amended; the *Securities Act*, RSNS 1989, c 418, as amended; the *Securities Act*, S Nu 2008, c 12, as amended; the *Securities Act*, RSPEI 1988, c S-3.1, as amended; the *Securities Act*, RSQ c V-1.1, as amended; the *Securities Act, 1988*, SS 1988-89, c S-42.2, as amended; and the *Securities Act*, SY 2007, c 16, as amended;
- (ss) “**Sino**” means the defendant, Sino-Forest Corporation;
- (tt) “**TD**” means the defendant TD Securities Inc.;
- (uu) “**TSX**” means the Toronto Stock Exchange;
- (vv) “**Underwriters**” means **Credit Suisse, Scotia, TD, Dundee, RBC, CIBC, Merrill, Canaccord and Maison**, collectively;
- (ww) “**Wang**” means the defendant Peter Wang;
- (xx) “**West**” means the defendant Garry J. West; and
- (yy) “**WFOE**” means wholly foreign owned enterprise or an enterprise established in China in accordance with the relevant PRC laws, with capital provided solely by foreign investors.

**CLAIM**

## 2. The Plaintiffs claim:

- (a) An order certifying this action as a class proceeding and appointing the Plaintiffs as representative plaintiffs for the Class, or such other class as may be certified by the Court;
- (b) A declaration that the Impugned Documents contained, either explicitly or implicitly, the Representation, and that, when made, the Representation was a misrepresentation, both at law and within the meaning of the Securities Legislation;
- (c) A declaration that the Impugned Documents contained one or more of the other misrepresentations alleged herein;
- (d) A declaration that Sino is vicariously liable for the acts and/or omissions of the Individual Defendants and of its other officers, directors and employees;
- (e) A declaration that the Underwriters, E&Y and Pöyry are each vicariously liable for the acts and/or omissions of their respective officers, directors, partners and employees;
- (f) On behalf of all of the Class Members who purchased Sino securities in the secondary market during the Class Period, and as against all of the Defendants other than the Underwriters, general damages in the sum of \$6.5 billion;
- (g) On behalf of all of the Class Members who purchased Sino common shares in the distribution to which the June 2007 Prospectus related, and as against all of the Defendants who signed the June 2007 Prospectus, general damages in the sum of \$175,835,000;
- (h) On behalf of all of the Class Members who purchased Sino common shares in the distribution to which the June 2009 Prospectus related, and as against all of the Defendants who signed the June 2009 Prospectus, general damages in the sum of \$330,000,000;

- (i) On behalf of all of the Class Members who purchased Sino common shares in the distribution to which the December 2009 Prospectus related, and as against all of the Defendants who signed the December 2009 Prospectus, general damages in the sum of \$319,200,000;
- (j) On behalf of all of the Class Members, and as against Sino, Chan, Poon and Horsley, punitive damages, in respect of the conspiracy pled below, in the sum of \$50 million;
- (k) A declaration that Sino, Chan, Martin, Poon, Horsley, Mak, Murray and the Underwriters were unjustly enriched;
- (l) A constructive trust, accounting or such other equitable remedy as may be available as against Sino, Chan, Martin, Poon, Horsley, Mak, Murray and the Underwriters;
- (m) A declaration that the acts and omissions of Sino have effected a result, the business or affairs of Sino have been carried on or conducted in a manner, or the powers of the directors of Sino have been exercised in a manner, that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of the Plaintiffs and the Class Members, pursuant to s. 241 of the *CBCA*;
- (n) An order directing a reference or giving such other directions as may be necessary to determine the issues, if any, not determined at the trial of the common issues;
- (o) Leave to amend this pleading to assert the causes of action set out in Part XXIII.1 of the *OSA* and, if necessary, the equivalent sections of the Securities Legislation other than the *OSA*;
- (p) Prejudgment and post judgment interest;
- (q) Costs of this action on a substantial indemnity basis or in an amount that provides full indemnity plus, pursuant to s 26(9) of the *CPA*, the costs of notice and of administering the plan of distribution of the recovery in this action plus applicable taxes; and

- (r) Such further and other relief as to this Honourable Court may seem just.

### OVERVIEW

3. From the time of its establishment in 1994, Sino has claimed to be a legitimate business operating in the commercial forestry industry in the PRC and elsewhere. Throughout that period, Sino has also claimed to have experienced breathtaking growth.

4. From 1994 to 2010, Sino's reported annual revenues increased from US\$20.5 million to US\$1.9 billion, or 9,291%, and its year-over-year reported revenues decreased only *once*, in 2000. During that same period, Sino's reported net income increased from US\$3.0 million to US\$395.4 million, or 13,037%, and its year-over-year reported net annual income decreased only twice, in 2000 and 2001. Finally, from 1994 to 2010, Sino's reported total assets as at year-end increased from US\$30.6 million to US\$5.7 billion, or 18,616%. During that period, Sino's year-over-year reported assets *never* decreased.

5. Compared to forestry companies identified by Sino as its peers, and indeed by any rational measure, Sino's growth and reported results have been simply unnatural.

6. For *none* of the sixty quarters comprising the years 1996 to 2010 did Sino report a net loss; rather, for *100%* of all such quarters, Sino reported significant net income.

7. During the same period, the results of Sino's peer companies were far less impressive. Norbord Inc. reported a net loss with respect to 37% of the quarters for which it disclosed results during the period 1996 to 2010. For Western Forest Products Inc., Ainsworth Lumber Company Ltd., Mercer International Inc. and International Forest Products Limited, the figure was, respectively, 63%, 49%, 54% and 39%. And finally; Cathay Forest Products Corp., another

Canadian public forestry company with operations in the PRC, reported a net loss in 96% of the quarters for which it disclosed financial results in that period.

8. Beguiled by Sino's reported results, and by Sino's constant refrain that China constituted an extraordinary growth opportunity, investors drove Sino's stock price dramatically higher, as appears from the following chart:



9. The Defendants profited handsomely from the market's resulting appetite for Sino's securities. Certain of the Individual Defendants sold Sino shares at lofty prices, and thereby reaped millions of dollars of gains. Sino's senior management also used Sino's illusory success to justify their lavish salaries, bonuses and other perks. For certain of the Individual Defendants, these outsized gains were not enough. Namely, Sino stock options granted to Chan, Horsley and other insiders were backdated or otherwise mispriced, prior to and during the Class Period, in violation of the TSX Rules, GAAP and the Securities Legislation.

10. Sino itself raised in excess of \$2.7 billion<sup>1</sup> in the capital markets during this period. Meanwhile, the Underwriters were paid lucrative underwriting commissions, and E&Y and Pöyry garnered millions of dollars in fees to bless Sino's reported results and assets. To their great detriment, the Class Members relied upon these supposed gatekeepers.

11. As a reporting issuer in Ontario and elsewhere, Sino was required at all material times to comply with GAAP. Indeed, Sino and E&Y, Sino's auditor during the Class Period and previously, repeatedly misrepresented that Sino's financial statements complied with GAAP. This was false.

12. On June 2, 2011, Muddy Waters, a short seller and research firm with extensive PRC experience, issued its first research report in relation to Sino, and unveiled the scale of the deception that had been worked upon the Class Members. Muddy Waters' initial report effectively revealed, among other things, that Sino had materially misstated its financial results, had falsely claimed to have acquired trees that it did not own, had reported sales that had not been made, or that had been made in a manner that did not permit Sino to book those sales as revenue under GAAP, and had concealed numerous related party transactions. These revelations had a catastrophic effect on Sino's stock price.

13. On June 1, 2011, prior to the publication of Muddy Waters' report, Sino's common shares closed at \$18.21. After the Muddy Waters report became public, Sino shares fell to \$14.46 on the TSX (a decline of 20.6%), at which point trading was halted. When trading resumed the next day, Sino's shares fell to a close of \$5.23 (a decline of 71.3% from June 1).

14. On Saturday June 18 and Sunday June 19, 2011, the *Globe* published investigatory articles that revealed, among other things, that Sino had "substantially overstated the size and

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<sup>1</sup> Dollar figures are in Canadian dollars (unless otherwise indicated) and are rounded for convenience.



value of its forestry holdings in China's Yunnan province." When the market closed on Monday, June 20, 2011, Sino's shares were trading at \$2.73 (a decline of 85% from June 1). After the close of markets on June 20, it was revealed that certain entities affiliated with Paulson & Co., which had been Sino's largest shareholder, had sold all of their holdings (realizing a loss, on a mark-to-market basis, in excess of US\$560 million). The next day, Sino shares closed at \$1.99, a decline of \$16.22 or 89.1% from its close on June 1. The value of other Sino securities, including various debt instruments, also sustained material declines.

15. Finally, on August 26, 2011, the OSC cease-traded Sino's securities, alleging that Sino appeared to have engaged in significant non-arm's length transactions which may have been contrary to Ontario securities laws and the public interest, that Sino and certain of its officers and directors appeared to have misrepresented some of Sino's revenue and/or exaggerated some of its timber holdings, and that Sino and certain of its officers and directors, including Chan, appeared to be engaging or participating in acts, practices or a course of conduct related to Sino's securities which they (or any of them) knew or ought reasonably know would perpetuate a fraud.

16. This action is now brought to recover the Class Members' losses from those who caused them: the Defendants.

## **THE PARTIES**

### ***The Plaintiffs***

17. Labourers are the trustees of the Labourers' Pension Fund of Central and Eastern Canada, a multi-employer pension plan providing benefits for employees working in the construction industry. The fund is a union-negotiated, collectively-bargained defined benefit pension plan established on February 23, 1972 and currently has approximately \$2 billion in assets, over 39,000 members and over 13,000 pensioners and beneficiaries and approximately 2,000

participating employers. A board of trustees representing members of the plan governs the fund. The plan is registered under the *Pension Benefits Act*, RSO 1990, c P.8 and the *Income Tax Act*, RSC 1985, 5th Supp, c.1.

18. Operating Engineers are the trustees of the International Union of Operating Engineers Local 793 Pension Plan for Operating Engineers in Ontario, a multi-employer pension plan providing pension benefits for operating engineers in Ontario. The pension plan is a union-negotiated, collectively-bargained defined benefit pension plan established on November 1, 1973 and currently has approximately \$1.5 billion in assets, over 9,000 members and pensioners and beneficiaries. The fund is governed by a board of trustees representing members of the plan. The plan is registered under the *Pension Benefits Act*, RSO 1990, c P.8 and the *Income Tax Act*, RSC 1985, 5th Supp, c.1.

19. The Plaintiffs purchased Sino shares over the TSX during the Class Period.

20. In addition, Labourers purchased Sino shares pursuant to the December 2009 Prospectus.

### ***The Defendants***

21. The Defendant Sino purports to be a commercial forest plantation operator in the PRC and elsewhere. Sino is a corporation formed under the *CBCA*.

22. At the material times, Sino was a reporting issuer in all provinces of Canada, and had its registered office located in Mississauga, Ontario. At the material times, Sino's shares were listed for trading on the TSX under the ticker symbol "TRE," on the Berlin exchange as "SFJ GR," on the OTC market in the United States as "SNOFF" and on the Tradedgate market as "SFJ TH." Sino securities are also listed on alternative trading venues in Canada and elsewhere including, without limitation, AlphaToronto and PureTrading. Sino has various debt instruments, derivatives and other securities that are traded in Canada and elsewhere.

23. As a reporting issuer in Ontario, Sino was required throughout the Class Period to issue and file with SEDAR:

- (a) within 45 days of the end of each quarter, quarterly interim financial statements prepared in accordance with GAAP that must include a comparative statement to the end of each of the corresponding periods in the previous financial year;
- (b) within 90 days of the end of the fiscal year, annual financial statements prepared in accordance with GAAP, including comparative financial statements relating to the period covered by the preceding financial year;
- (c) contemporaneously with each of the above, a MD&A of each of the above financial statements; and
- (d) within 90 days of the end of the fiscal year, an AIF, including material information about the company and its business at a point in time in the context of its historical and possible future development.

24. MD&As are a narrative explanation of how the company performed during the period covered by the financial statements, and of the company's financial condition and future prospects. The MD&A must discuss important trends and risks that have affected the financial statements, and trends and risks that are reasonably likely to affect them in future.

25. AIFs are an annual disclosure document intended to provide material information about the company and its business at a point in time in the context of its historical and future development. The AIF describes the company, its operations and prospects, risks and other external factors that impact the company specifically.

26. Chan is a co-founder of Sino, and has been the Chairman, Chief Executive Officer and a director of the company since 1994. As Sino's CEO, Chan signed and certified the company's

disclosure documents during the Class Period. Chan, along with Hyde, signed each of the 2006-2010 Annual Consolidated Financial Statements on behalf of Sino's board. Chan resides in Hong Kong.

27. Shortly after Sino was established in 1994, Sino began to report that Chan had been a Director of A. D. Sinensis & Associates Ltd. ("Sinensis"), a "project financing and management consultancy," from August 1991 to August 1993. In fact, Chan did not become a director of Sinensis until October 1993. Sino has never disclosed this fact, nor has it ever disclosed what Chan's true occupation was during that period.

28. In addition, from the time that Sino was established, Sino has touted Chan's connections to, and good relations with, the government of the PRC. For example, in Sino's inaugural Proxy Circular of February 11, 1994 (the "Initial Proxy Circular"), Chan was described as having served as a "senior economic adviser" to the Ministry of Foreign Economic Relations and Trade of the PRC. Sino never disclosed, however, that in 1990, Chan and New Ross Investments Limited, a Hong Kong company of which Chan was then a director and majority shareholder ("New Ross"), were named as defendants in a proceeding filed in Hong Kong by a Chinese government organization, the China Foreign Trade Leasing Corporation ("CFTLC").

29. In that proceeding, CFTLC alleged it had entered into agreements with New Ross and Chan pursuant to which CFTLC would loan New Ross approximately US\$650,000, New Ross would use the funds solely for the purpose of purchasing the equity of a shipyard company, New Ross would repay the principal within eight months, with interest, and Chan would guarantee the obligation of New Ross. CFTLC further alleged that, after New Ross failed to repay the principal and interest within eight months, New Ross informed CFTLC that the funds had not

been used for the specified purpose. CFTLC nonetheless agreed to an extension of the time for New Ross to satisfy its obligations to CFTLC. CFTLC alleged that, in purported discharge of part of his liability to CFTLC, Chan issued two cheques drawn upon the Hongkong and Shanghai Banking Corporation in the aggregate amount of HK\$1 million, but that those cheques were dishonoured upon presentation.

30. Since Sino was established, Chan has received lavish compensation from Sino. For example, for 2006 to 2010, Chan's total compensation (other than share-based compensation) was, respectively, US\$3.0 million, US\$3.8 million, US\$5.0 million, US\$7.6 million and US\$9.3 million.

31. As at May 1, 1995, shortly after Sino became a reporting issuer, Chan held 18.3% of Sino's outstanding common shares and 37.5% of its preference shares. As of April 29, 2011 he held 2.7% of Sino's common shares (the company no longer has preference shares outstanding). Chan has made in excess of \$10 million through the sale of Sino shares.

32. Horsley is Sino's Chief Financial Officer, and has held this position since October 2005. In his position as Sino's CFO, Horsley has signed and certified the company's disclosure documents during the Class Period. Horsley resides in Ontario. Horsley has made in excess of \$11 million through the sale of Sino shares.

33. Since becoming Sino's CFO, Horsely too has received lavish compensation from Sino. For 2006 to 2010, Horsley's total compensation (other than share-based compensation) was, respectively, US\$1.1 million, US\$1.4 million, US\$1.7 million, US\$2.5 million, and US\$3.1 million.

34. Poon is a co-founder of Sino, and has been the President of the company since 1994. He was a director of Sino from 1994 to May 2009, and he continues to serve as Sino's President. Poon resides in Hong Kong.

35. Beginning with Sino's Initial Proxy Circular, Poon claimed to have graduated from "Guangzhou Chungnam Forestry University" in 1962. However, no such university exists.

36. As at May 1, 1995, shortly after Sino became a reporting issuer, Poon held 18.3% of Sino's outstanding common shares and 37.5% of its preference shares. As of April 29, 2011 he held 0.42% of Sino's common shares. Poon has made in excess of \$34.4 million through the sale of Sino shares.

37. Poon rarely attended board meetings while he was on Sino's board. From the beginning of 2006 until his resignation from the Board in 2009, he attended 5 of the 39 board meetings, or less than 13% of all board meetings held during that period.

38. Wang is a director of Sino, and has held this position since August 2007. Wang resides in Hong Kong.

39. Martin served as a director of Sino from 2006 to June 2010. He was appointed as the company's Vice-Chairman in 2010 and continues to hold this position. Martin was a member of Sino's audit committee prior to early 2011. Martin has made in excess of \$474,000 through the sale of Sino shares. He resides in Hong Kong.

40. Mak is a director of Sino, and has held this position since 1994. Mak was a member of Sino's audit committee prior to early 2011. Mak and persons connected with Mak have made in excess of \$6.4 million through sales of Sino shares. Mak resides in British Columbia.

41. Murray is a director of Sino, and has held this position since 1999. Murray has made in excess of \$9.9 million through sales of Sino shares. Murray resides in Hong Kong.

42. Since becoming a director, Murray has rarely attended board and board committee meetings. From the beginning of 2006 to the close of 2010, Murray attended 14 of 64 board meetings, or less than 22% of board meetings held during that period. During that same period, Murray attended 2 out of 13, or 15%, of the meetings held by the Board's Compensation and Nominating Committee, and attended *none* of the 11 meetings of that Committee held from the beginning of 2007 to the close of 2010.

43. Hyde is a director of Sino, and has held this position since 2004. Hyde was previously a partner of E&Y. Hyde is the chairman of Sino's Audit Committee. Hyde, along with Chan, signed each of the 2007-2010 Annual Consolidated Financial Statements on behalf of Sino's board. Hyde is also member of the Compensation and Nominating Committee. Hyde has made in excess of \$2.4 million through the sale of Sino shares. Hyde resides in Ontario.

44. Ardell is a director of Sino, and has held this position since January 2010. Ardell is a member of Sino's audit committee. Ardell resides in Ontario.

45. Bowland is a director of Sino, and has held this position since February 2011. Bowland is a member of Sino's Audit Committee and was formerly an employee or partner of E&Y. Bowland resides in Ontario.

46. West is a director of Sino, and has held this position since February 2011. West was previously a partner at E&Y. West is a member of Sino's Audit Committee. West resides in Ontario.

47. At all material times, Sino maintained the Code, which governed Sino's employees, officers and directors, including the Individual Defendants. The Code stated that the members of senior management "are expected to lead according to high standards of ethical conduct, in both words and actions..." The Code further required that Sino representatives act in the best interests of shareholders, corporate opportunities not be used for personal gain, no one trade in Sino securities based on undisclosed knowledge stemming from their position or employment with Sino, the company's books and records be honest and accurate, conflicts of interest be avoided, and any violations or suspected violations of the Code, and any concerns regarding accounting, financial statement disclosure, internal accounting or disclosure controls or auditing matters, be reported.

48. E&Y has been engaged as Sino's auditor since August 13, 2007. E&Y was also engaged as Sino's auditor from Sino's creation through February 19, 1999, when E&Y abruptly resigned during audit season and was replaced by the now-defunct Arthur Andersen LLP. E&Y was also Sino's auditor from 2000 to 2004, when it was replaced by the auditing firm BDO McCabe ("BDO"). E&Y is an expert of Sino within the meaning of the Securities Legislation.

49. E&Y, in providing what it purported to be "audit" services to Sino, made statements that it knowingly intended to be, and which were, disseminated to Sino's current and prospective security holders. At all material times, E&Y was aware of that class of persons, intended to and did communicate with them, and intended that that class of persons would rely on E&Y's statements relating to Sino, which they did to their detriment.

50. Pöyry is an international forestry consulting firm which purported to provide certain forestry consultation services to Sino. Pöyry is an expert of Sino within the meaning of the Securities Legislation.



51. Pöyry, in providing (or claiming to provide) “forestry consulting” services to Sino, made statements that it knowingly intended to be, and which were, disseminated to Sino’s current and prospective security holders. At all material times, Pöyry was aware of that class of persons, intended to and did communicate with them, and intended that that class of persons would rely on Pöyry’s statements relating to Sino, which they did to their detriment.

52. The Underwriters are various financial institutions who served as underwriters in one or more of the offerings made pursuant to the June 2007, June 2009 and/or December 2009 Prospectuses. In connection with the distributions conducted pursuant to the June 2007, June 2009 and December 2009 Prospectuses, the Underwriters who underwrote those distributions were paid, respectively, an aggregate of approximately \$7.5 million, \$14.0 million and \$14.4 million in underwriting commissions. Those commissions were paid in substantial part as consideration for the Underwriters’ purported due diligence examination of Sino’s business and affairs.

#### **SINO ACCESSES ONTARIO’S CAPITAL MARKETS**

53. Sino conducted three prospectus offerings during the Class Period, and various private placements and other transactions, raising in aggregate in excess of \$2.7 billion from investors (collectively, the “**Offerings**”). In particular:

- (a) On June 5, 2007, Sino issued and filed with SEDAR the June 2007 Prospectus pursuant to which Sino distributed to the public 15,900,000 common shares at a price of \$12.65 per share for gross proceeds of \$201,135,000. The June 2007 Prospectus incorporated by reference certain of Sino’s disclosure documents, including the: (1) 2006 AIF; (2) 2006 Annual Audited Financial Statements; (3) 2006 Annual MD&A; (4) Management Information Circular dated April 27, 2007; (5) Q1 2007 Financial Statements; and (6) Q1 2007 MD&A;

- (b) On or about July 23, 2008, Sino issued a final “Offering Memorandum” pursuant to which Sino sold through private placement US\$345 million in aggregate principal amount of convertible senior notes due 2013;
- (c) On June 1, 2009, Sino issued and filed with SEDAR the June 2009 Prospectus pursuant to which Sino distributed to the public 34,500,000 common shares at a price of \$11.00 per share for gross proceeds of \$379,500,000. The June 2009 Prospectus incorporated by reference certain of Sino’s disclosure documents, including the: (1) 2008 AIF; (2) 2007 and 2008 Annual Consolidated Financial Statements; (3) Amended 2008 Annual MD&A; (4) Q1 2009 MD&A; (5) Q1 2008 and 2009 Financial Statements; (6) Q1 2009 MD&A; (7) Management Information Circular dated April 28, 2009; and (8) the Pöyry report titled “Valuation of China Forest Corp Assets As at 31 December 2008;”
- (d) On June 24, 2009, Sino issued and filed with SEDAR an Exchange Offer Memorandum for exchange of certain of its then outstanding senior notes with new notes, pursuant to which Sino issued US\$212,330,000 in aggregate principal amount of guaranteed senior notes due 2014;
- (e) On December 10, 2009, Sino issued a final Offering Memorandum pursuant to which Sino sold through private placement US\$460,000,000 in aggregate principal amount of convertible senior notes due 2016. This Offering Memorandum incorporated by reference the Pöyry reports entitled “Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2007” and “Sino-Forest Corporation Valuation of China Forest Corp Assets as at 31 December 2008;”
- (f) On December 11, 2009, Sino issued and filed with SEDAR the December 2009 Prospectus (together with the June 2007 Prospectus and the June 2009 Prospectus, the “**Prospectuses**”) pursuant to which Sino distributed to the public 21,850,000 common shares at a price of \$16.80 per share for gross proceeds of \$367,080,000. The December 2009 Prospectus incorporated by reference certain of Sino’s disclosure documents, including: (1) the 2008 AIF; (2) the 2007 and 2008 Annual

Consolidated Financial Statements; (3) the Amended 2008 Annual MD&A; (4) the Q3 2008 and 2009 Financial Statements; (5) the Q3 2009 MD&A; (6) the Management Information Circular dated April 28, 2009; and (7) the Pöyry report titled “Valuation of China Forest Corp Assets As at 31 December 2008;”

- (g) On February 8, 2010, Sino closed the acquisition of substantially all of the outstanding common shares of Mandra Forestry Holdings Limited. Concurrent with this acquisition, Sino completed an exchange with holders of 99.7% of the USD\$195 million notes issued by Mandra Forestry Finance Limited and 96.7% of the warrants issued by Mandra Forestry Holdings Limited, for new guaranteed senior notes issued by Sino in the aggregate principal amount of USD\$187,177,375 with a maturity date of July 28, 2014. On February 11, 2010, Sino exchanged the New 2014 Senior Notes for an additional issue of USD\$187,187,000 in aggregate principal amount of Sino’s existing 2014 Senior Notes; and
- (h) On October 14, 2010, Sino issued a final Offering Memorandum pursuant to which Sino sold through private placement US\$600,000,000 in aggregate principal amount of guaranteed senior notes due 2017.

54. The offering documents referenced in the preceding paragraph included, or incorporated other documents by reference that included, the Representation and the other misrepresentations in such documents that are particularized elsewhere herein. Had the truth in regard to Sino’s management, business and affairs been timely disclosed, securities regulators likely would not have receipted the Prospectuses, nor would the Offerings have occurred.

55. Each of Chan, Horsley, Martin, Hyde, Poon, Mak and Murray signed the June 2007 Prospectus, and therein falsely certified that that prospectus, together with the documents incorporated therein by reference, constituted full, true and plain disclosure of all material facts relating to the securities offered thereby. Each of Dundee, CIBC, Merrill and Credit Suisse also

signed the June 2007 Prospectus, and therein falsely certified that, to the best of its knowledge, information and belief, that prospectus, together with the documents incorporated therein by reference, constituted full, true and plain disclosure of all material facts relating to the securities offered thereby.

56. Each of Chan, Horsley, Martin, Mak, Murray, Hyde and Wang signed the June 2009 Prospectus, and therein falsely certified that that prospectus, together with the documents incorporated therein by reference, constituted full, true and plain disclosure of all material facts relating to the securities offered thereby. Each of Dundee, Merrill, Credit Suisse, Scotia and TD also signed the June 2009 Prospectus, and therein falsely certified that, to the best of its knowledge, information and belief, that prospectus, together with the documents incorporated therein by reference, constituted full, true and plain disclosure of all material facts relating to the securities offered thereby.

57. Each of Chan, Horsley, Martin, Mak, Murray, Hyde and Wang signed the December 2009 Prospectus, and therein falsely certified that that prospectus, together with the documents incorporated therein by reference, constituted full, true and plain disclosure of all material facts relating to the securities offered thereby. Each of Dundee, Merrill, Credit Suisse, Scotia, CIBC, RBC, Maison, Canaccord and TD also signed the December 2009 Prospectus, and therein falsely certified that, to the best of its knowledge, information and belief, that prospectus, together with the documents incorporated therein by reference, constituted full, true and plain disclosure of all material facts relating to the securities offered thereby.

58. E&Y consented to the inclusion in the June 2009 and December 2009 Prospectuses of its audit reports on Sino's Annual Audited Financial Statements for 2008 and 2007.

## SINO'S ORIGINS

59. At the time of its establishment, Sino purported to be in the business of acquiring forestry land rights and processing and selling wood chips in the PRC, both directly and through various joint ventures.

60. Sino's reported revenues, income and assets thereafter grew rapidly as it transacted earlier and earlier in the overall business cycle, and as Sino became increasingly complex. By the early 2000s, Sino business structure had changed to include wholly-owned subsidiaries and so-called authorized intermediaries ("AIs").

61. In its Initial Proxy Circular, Sino purported to operate through six joint ventures formed in the PRC. By early 2011, Sino purported to conduct business through well over 60 subsidiaries, at least 16 of which were formed in the British Virgin Islands ("BVI"), and at least 40 of which were formed in the PRC.

62. Sino's complicated and constantly changing structure, the appearance of arm's-length intermediaries and its carefully crafted purchase and sale agreements combined with the effect that consistently high profit margins could be reported, auditor sign-offs could be achieved, certain taxes could be minimized or not paid, and asset valuations could be obtained from experts claimed to be independent.

63. Thus, the now legitimized and rapidly growing business could be packaged to raise roughly \$1 billion in equity and \$1.8 billion in debt financing, while insiders were enriched through the exercise of stock options (including mispriced stock options), salaries and benefits, consulting fees and other means.

64. This scheme occurred in the backdrop of related party, taxation and revenue recognition disclosures that were false and incomplete, and violated GAAP.

65. Sino's entrance into Canada's capital markets was effected by means of a "reverse takeover." In a reverse takeover, a public shell company acquires a private company that is seeking to become public. The private company (Sino, in this case) becomes public without the scrutiny of an IPO.

66. The defendants Chan (identified as Tak Yuen Chan), Poon and Mak (along with John Thompson and James Francis O'Donnell) were the directors of Sino promptly following the reverse takeover. Chan was Chairman of the Board and CEO and Poon was President of the company. E&Y was appointed Sino's initial auditor.

67. The Hong Kong office of E&Y audited the 1993 Audited Financial Statements of Sino-Wood Partners, Limited, which were included in the February 11, 1994 Proxy Circular. Chan signed those financial statements. E&Y (Hong Kong) also "reviewed, as to compilation only" certain pro-forma statements of various Sino equity joint ventures, also included in that proxy circular. E&Y (Toronto) "reviewed, as to compilation only" the 1993 pro-forma consolidated balance sheet of Sino, also included in that circular.

***Sino Overstates the Value of, and the Revenues Generated by, the Leizhou Joint Venture***

68. Initially, Sino's business was conducted primarily through an equity joint venture with the Leizhou Forestry Bureau, which was situated in Guangdong Province in the south of the PRC. The name of the venture was Zhanjiang Leizhou Eucalyptus Resources Development Co. Ltd. ("**Leizhou**"). The stated purpose of Leizhou, established in 1994, was:

Managing forests, wood processing, the production of wood products and wood chemical products, and establishing a production facility with an annual production capacity of 50,000 m<sup>3</sup> of Micro Density Fiber Board (MDF), managing a base of 120,000 mu (8,000 ha) of which the forest annual utilization would be 8,000 m<sup>3</sup>.

69. There are two types of joint ventures in the PRC relevant to Sino: equity joint ventures (“EJV”) and cooperating joint ventures (“CJV”). In an EJV, profits and assets are distributed in proportion to the parties’ equity holdings upon winding up. In a CJV, the parties may contract to divide profits and assets disproportionately to their equity interests.

70. According to a Sino prospectus issued in January 1997, Leizhou, an EJV, was responsible for 20,000 hectares of the 30,000 hectares that Sino claimed to have “phased-in.” Leizhou was thus the key driver of Sino’s purported early growth.

71. Sino claimed to hold 53% of the equity in Leizhou, which was to total US\$10 million, and Sino further claimed that the Leizhou Forestry Bureau was to contribute 20,000 ha of forestry land. In reality, however, the terms of the EJV required the Leizhou Forestry Bureau to contribute a mere 3,533 ha.

72. What was also unknown to investors was that Leizhou did not generate the sales claimed by Sino. More particularly, in 1994, 1995 and 1996, respectively, Sino claimed to have generated US\$11.3 million, US\$23.9 million and US\$23.1 million in sales from Leizhou. In reality, however, these sales did not occur, or were materially overstated.

73. Indeed, in an undisclosed letter from Leizhou Forestry Bureau to Zhanjiang City Foreign and Economic Relations and Trade Commission, dated February 27, 1998, the Bureau complained:

***The Joint Venture is not capable of operation***

According to the contract and charter, the main purposes of setting up the Joint Venture are, on the one hand, to invest and construct a project producing 50,000 cubic meter Medium Density Fiberboard (MDF) a year; on the other hand, to create a forest base of 120,000 mu, with which to produce 80,000 cubic meter of timber as raw material for the production of medium density fiberboard. The contract and charter also prescribed that the funding required for the MDF board project should be paid by the foreign party in cash; our side should pay in-kind

the proportion of the fund prescribed by the contract. After paying 1 million USD, ***the foreign party [Sino] not only failed to fully fund the company***, but also approved in their own name the gradual withdrew of funds in the amount of RMB 4,141,045.02 RMB [approximately \$500,000], from the paid in capital provided by their company for the Joint Venture, among which \$270,000 USD was paid out to the Huadu Baixing Wood Products Factory, which has had no business relationship with the joint venture at all. This amount of money equals 47.6% of the money [Sino] paid in capital. Although our side has almost paid off the subscribed capital (only short 0.9% of the total committed), because of the limited contribution from the foreign party, and withdrew a huge amount of money from among those funds originally contributed by the foreign party, ***it is impossible to put into practice the project that the joint venture aimed to construct or set up and the intended production and business operation activities. This is all because the funds have been insufficient and the foreign party did not pay in the majority of the subscribed capital. The joint venture therefore is merely a shell, existing in name only.***

Additionally, after the establishment of the Joint Venture, ***the internal operations have been extremely abnormal***, for example, annual board meetings have not been held as scheduled; annual reports on the status and results of annual finance auditing are missing; the huge amount of funds withdrawn by the foreign party were not discussed in the board meeting, etc. It is hard to list all the improper operations here.

[Translation; emphasis added.]

74. In its 1996 Annual Financial Statements, Sino stated:

The \$14,992,000 due from the LFB represents cash collected from the sale of wood chips on behalf of the Leizhou EJV. As originally agreed to by Sino-Wood, the cash was being retained by the LFB to fund the ongoing plantation costs of the Leizhou EJV incurred by the LFB. Sino-Wood and LFB have agreed that the amount due to the Leizhou EJV, after reduction for plantation costs incurred, will be settled in 1997 concurrent with the settlement of capital contributions due to the Leizhou EJV by Sino-Wood.

75. These statements were false, inasmuch as Leizhou never generated such sales. Leizhou was wound-up in 1998.

#### ***Sino's Fictitious Investment in SJXT***

76. In Sino's audited financial statements for the year ended December 31, 1997, filed on SEDAR on May 20, 1998 (the "1997 Financial Statements"), Sino stated that, in order to



establish strategic partnerships with key local wood product suppliers and to build a strong distribution for the wood-based product and contract supply businesses, it had acquired a 20% equity interest in “Shanghai Jin Xiang Timber Ltd.” (“SJXT”). Sino then described SJXT as an EJV that had been formed in 1997 by the Ministry of Forestry in China, and declared that its function was to organize and manage the first and only official market for timber and log trading in Eastern China. It further stated that the investment in SJXT was expected to provide the Company with good accessibility to a large base of potential customers and companies in the timber and log businesses in Eastern China.

77. According to the 1997 Financial Statements, the total investment of SJXT was estimated to be US\$9.7 million, of which Sino would be required to contribute approximately US\$1.9 million for a 20% equity interest. The 1997 Financial Statements stated that, as at December 31, 1997, Sino had made capital contributions to SJXT in the amount of US\$1.0. In Sino’s balance sheet as at December 31, 1997, the SJXT investment was shown as an asset of \$1.0 million.

78. In October 1998, Sino announced an Agency Agreement with SJXT. At that time, Sino stated that it would provide 130,000 m<sup>3</sup> of various wood products to SJXT over an 18 month period, and that, based on then-current market prices, it expected this contract to generate “significant revenue” for Sino-Forest amounting to approximately \$40 million. The revenues that were purportedly anticipated from the SJXT contract were highly material to Sino. Indeed, Sino’s total reported revenues in 1998 were \$92.7 million.

79. In Sino’s audited financial statements for the year ended December 31, 1998, which statements were filed on SEDAR on May 18, 1999 (the “1998 Financial Statements”), Sino again stated that, in 1997, it had acquired a 20% equity interest in SJXT, that the total investment in SJXT was estimated to be US\$9.7 million, of which Sino would be required to contribute

approximately \$1.9 million, representing 20% of the registered capital, and that, as at December 31, 1997 and 1998, Sino had made contributions in the amount of US\$1.0 million to SJXT. In Sino's balance sheet as at December 31, 1998, the SJXT investment was again shown as an asset of US\$1.0 million.

80. Sino also stated in the 1998 Financial Statements that, during 1998, the sale of logs and lumber to SJXT amounted to approximately US\$537,000. These sales were identified in the notes to the 1998 Financial Statements as related party transactions.

81. In Sino's Annual Report for 1998, Chan stated that lumber and wood products trading constituted a "promising new opportunity." Chan explained that:

*SJXT represents a very significant development for our lumber and wood products trading business. The market is prospering and continues to look very promising.* Phase I, consisting of 100 shops, is completed. Phases II and III are expected to be completed by the year 2000. This expansion would triple the size of the Shanghai Timber Market.

*The Shanghai Timber Market is important to Sino-Forest as a generator of significant new revenue. In addition to supplying various forest products to the market from our own operations, our direct participation in SJXT increases our activities in sourcing a wide range of other wood products both from inside China and internationally.*

*The Shanghai Timber Market is also very beneficial to the development of the forest products industry in China because it is the first forest products national sub-market in the eastern region of the country.*

[...]

*The market also greatly facilitates Sino-Forest's networking activities, enabling us to build new industry relationships and add to our market intelligence, all of which increasingly leverage our ability to act as principal in our dealings.*

[Emphasis added.]

82. Chan also stated in the 1998 Annual Report that the "Agency Agreement with SJXT [is] expected to generate approximately \$40 million over 18 months."

83. In Sino's Annual Report for 1999, Sino stated:

*There are also promising growth opportunities as Sino-Forest's investment in Shanghai Jin Xiang Timber Ltd. (SJXT or the Shanghai Timber Market), develops.* The Company also continues to explore opportunities to establish and reinforce ties with other international forestry companies and to bring our e-commerce technology into operation.

Sino-Forest's investment in the Shanghai Timber Market — the first national forest products submarket in eastern China — has provided a strong foundation for the Company's lumber and wood products trading business.

[Emphasis added.]

84. In Sino's MD&A for the year ended December 31, 1999, Sino also stated that:

*Sales from lumber and wood products trading increased 264% to \$34.2 million compared to \$9.4 million in 1998. The increase in lumber and wood products trading is attributable largely to the increase in new business generated from our investment in Shanghai Jin Xiang Timber Ltd. (SJXT) and a larger sales force in 1999.* Lumber and wood products trading on an agency basis has increased 35% from \$2.3 million in 1998 to \$3.1 million in 1999. The increase in commission income on lumber and wood products trading is attributable to approximately \$1.8 million of fees earned from a new customer.

[Emphasis added.]

85. In Sino's audited annual financial statements for the year ended December 31, 1999, which statements were filed on SEDAR on May 18, 2000 (the "1999 Financial Statements"), Sino stated:

During the year, Shanghai Jin Xiang Timber Ltd. ["SJXT"] applied to increase *the original total capital contributions of \$868,000* [Chinese renminbi 7.2 million] to \$1,509,000 [Chinese renminbi 12.5 million]. Sino-Wood is required to *make an additional contribution of \$278,000* as a result of the increase in total capital contributions. The additional capital contribution of \$278,000 was made in 1999 *increasing its equity interest in SJXT from 27.8% to 34.4%*. The principal activity of SJXT is to organize trading of timber and logs in the PRC market.

[Emphasis added.]

86. The statements made in the 1999 Financial Statements contradicted Sino's prior representations in relation to SJXT. Among other things, Sino previously claimed to have made a capital contribution of \$1,037,000 for a 20% equity interest in SJXT.

87. In addition, note 2(b) to the 1999 Financial Statements stated that, "[a]s at December 31, 1999, \$796,000...advances to SJXT remained outstanding. The advances to SJXT were unsecured, non-interest bearing and without a fixed repayment date." Thus, assuming that Sino's contributions to SJXT were actually made, then Sino's prior statements in relation to SJXT were materially misleading, and violated GAAP, inasmuch as those statements failed to disclose that Sino had made to SJXT, a related party, a non-interest bearing loan of \$796,000.

88. In Sino's audited annual financial statements for the year ended December 31, 2000, which statements were filed on SEDAR on May 18, 2000 (the "2000 Financial Statements"), Sino stated:

In 1999, Shanghai Jin Xiang Timber Ltd. ("SJXT") applied to increase the original total capital contributions of \$868,000 [Chinese renminbi 7.2 million] to \$1,509,000 [Chinese renminbi 12.5 million]. Sino-Wood is required to make an additional contribution of \$278,000 as a result of the increase in total capital contributions. The additional capital contribution of \$278,000 was made in 1999 increasing its equity interest in SJXT from 27.8% to 34.4%. The principal activity of SJXT is to organize the trading of timber and logs in the PRC market. During the year, advances to SJXT of \$796,000 were repaid.

89. In Sino's balance sheet as at December 31, 2000, the SJXT investment was shown as an asset of \$519,000, being the sum of Sino's purported SJXT investment of \$1,315,000 as at December 31, 1999, and the \$796,000 of "advances" purportedly repaid to Sino by SJXT during the year ended December 31, 2000.

90. In Sino's Annual Reports (including the annual audited financial statements contained therein) for the years 2001 and beyond, there is no discussion whatsoever of SJXT. Indeed,

Sino's "promising" and "very significant" investment in SJXT simply evaporated, without explanation, from Sino's disclosure documents. In fact, and unbeknownst to the public, Sino never invested in a company called "Shanghai Jin Xiang Timber Ltd." Chan and Poon knew, or were reckless in not knowing of, that fact.

***Sino's Failure to Disclose the Alkaner Winding-up Petition***

91. On December 16, 2003, a BVI corporation, Alkaner Assets Ltd. ("Alkaner"), filed a petition in the High Court of Hong Kong for an order compelling the winding up Sino. Had the petition been granted, then a liquidator would have been appointed, and Sino would have been at risk of a termination of its business activities.

92. The petition was settled on terms unknown to the Plaintiffs. However, given the severity of the consequences of the granting of Alkaner's petition, the fact that Alkaner had filed such a petition was material, and ought to have been disclosed to Sino's shareholders. Yet Sino never disclosed the Alkaner petition.

***Sino's Increasing Reliance on Authorized Intermediaries***

93. In Sino's AIF for the year ended December 31, 2003 ("2003 AIF"), Sino first disclosed that, through Sino-Forest Resources, Inc. and Suri-Wood Inc., each an indirect wholly-owned subsidiary formed in the BVI, Sino had been engaging in standing timber and wood chips sales and trading activities with AIs.

94. Although Sino claimed prior to and during the Class Period that its AIs, whose identities Sino largely concealed, possessed the requisite PRC business licenses to engage in trading activities, in fact the AIs were unnecessary from an operational perspective and exposed Sino to extraordinary risks, particularly in relation to Sino's tax liabilities in the PRC. As alleged more particularly below, the Defendants misrepresented the true purpose of the AIs, and greatly understated the risks arising from Sino's reliance upon them.

95. According to the 2003 AIF, for the three years ended December 31, 2003, sales transactions with these AIs constituted approximately 56.5%, 57.9% and 51.2%, respectively, of Sino's revenue. Despite the fact that sales through AIs accounted for a majority of Sino's revenues in 2002 and 2001, Sino did not disclose its reliance on AIs in those years until the issuance of the 2003 AIF in May 2004.

96. The 2003 AIF further stated:

Our relationships with our authorized intermediaries are governed by master agreements ("Master Agreements"), as supplemented by certain operational procedures relating to the wood chips sales transactions (the "Operational Procedures"). Under the Master Agreements, as supplemented by the Operational Procedures, we appoint the authorized intermediaries to manage our wood chips trading transactions on our behalf. The authorized intermediaries agree to enter into contracts to purchase timber from suppliers, process the timber into wood chips and deliver wood chips to customers pursuant to sales contracts entered into between the authorized intermediaries and customers. We agree to reimburse the costs of the authorized intermediaries, including the cost of the purchase of raw timber, and to pay both a processing fee and a management fee, all of which are deducted from the sales proceeds of the wood chips [...]

The Operational Procedures delineate our and the authorized intermediaries' rights and obligations with respect to the purchase of raw timber, the processing of raw timber into wood chips and the sale of wood chips. *Under the Operational Procedures, the authorized intermediaries assume the risks and obligations relating to the raw timber from the time the raw timber is purchased until it is delivered to the respective authorized intermediary's premises. We assume all risks and obligations relating to the raw timber once it arrives at the premises of the authorized intermediary until it is processed into wood chips, except for any loss arising as a result of the authorized intermediary's default.* Once the raw timber is processed into wood chips, the authorized intermediary is responsible for selling wood chips to customers and it assumes all rights and obligations relating to the wood chips under its sales contracts with customers. *The Operational Procedures provide that the authorized intermediaries are responsible for selling wood chips to customers within time limits agreed between the relevant authorized intermediary and us, and that they assume all risks and obligations for failing to meet these delivery requirements.*

[...]

Because of the provisions in the Operational Procedures that specify when we and the authorized intermediary assume the risks and obligations relating to the raw timber or wood chips, as the case may be, we treat these transactions for accounting purposes as providing that we take title to the raw timber when it is delivered to the authorized intermediary. Title then passes to the authorized intermediary once the timber is processed into wood chips. *Accordingly, we treat the authorized intermediaries for accounting purposes as being both our suppliers and customers in these transactions.*

[Emphasis added.]

97. Sino made additional disclosure regarding its reliance on AIs in its AIF for the year ended December 31, 2004, wherein it stated:

Two of our British Virgin Islands subsidiaries, Sino-Forest Resources, Inc. and Suri-Wood Inc., have been responsible for the authorized sales in the PRC of standing timber from our purchased tree plantations and the logs, wood chips and wood-based products processed from timber sourced from third party suppliers. They have conducted these sales activities through authorized intermediaries in the PRC. *The amount we receive from these activities is on a net basis after withholding of applicable taxes by the authorized intermediaries. Because the authorized intermediaries are responsible for filing the tax returns with, and withholding or paying relevant taxes to, the PRC government in respect of these activities, the two British Virgin Islands subsidiaries generally have not had the necessary documentation to evidence the payment of PRC taxes to the relevant branch of the State Administration for Foreign Exchange.*

98. In Sino's AIF for the year ended December 31, 2005, Sino made limited and materially deficient disclosure in relation to the tax risks arising from its use of AIs:

In accordance with Income Tax Laws, foreign companies deriving income from sources in the PRC are subject to corporate income tax as a foreign investment enterprise. ***Under the terms of the master agreements, relevant sales and purchase contracts and commission agreements made with the AI, the AI are responsible for paying all PRC taxes on behalf of the BVI subsidiaries that arise from the Authorized Sales Activities, including but not limited to, corporate income tax, value-added tax and business tax. Accordingly, the BVI Subsidiaries are not required to and therefore did not directly pay any PRC taxes with respect to the profits earned in the PRC. The relevant income remitted to the Company should have already been taxed and not subject to additional PRC taxes.***

***If PRC tax authorities were to determine that the AI did not pay applicable PRC taxes as required on the Authorized Sales Activities on behalf of the BVI Subsidiaries, they may attempt to recover the applicable PRC taxes or any shortfall from the BVI Subsidiaries. Since the BVI Subsidiaries are unable to ascertain whether the AI have properly handled such tax settlements and/or able to recover relevant PRC taxes required to be paid by the BVI Subsidiaries from the AI, a provision for the corporate income tax at an amount representing management's best estimate of the amount the PRC tax authorities might seek to recover, is recognized in the financial statements each year.*** The yearly provision is reversed to the income statement after a period of three years based on management' best estimate of the liability. This means that the Company always maintains a three-year provision for tax on the profits earned from the Authorized Sales Activities of the three most recent years.

As at December 31, 2005 the balance of the provision for these tax related liabilities amounting to \$25,379,000 (2004 – \$17,936,000) was provided on the profits of the Authorized Sales Activities earned by the BVI Subsidiaries over the three previous years.

[...] Should the PRC tax authorities recover income tax, business tax and value-added tax directly from the BVI Subsidiaries, they might do so together with related tax surcharges and tax penalties on applicable income or profits of the Authorized Sales Activities from the BVI Subsidiaries for up to three years in practice. ***Under prevailing PRC tax rules, the tax surcharge is calculated at 0.05% per day on the tax amount overdue while the tax penalties can range from 50% to 500% of taxes underpaid. Under the Hong Kong tax regulations, assessments are open for up to six years in practice and tax penalties can be up to treble amount of the tax underpaid.***

[Emphasis added.]

99. However, in order to mitigate any concerns that investors may have had in relation to Sino's extensive use of AIs, Sino stated:

***We intend to reduce our reliance on authorized intermediaries going forward.*** Currently, Jia Yao WFOE engages in sales of wood chips and logs sourced from third parties in the PRC through authorized intermediaries in the PRC. We intended to transfer



Jia Yao WFOE from Sino-Panel (Gaoyao) Limited to Sino-Forest (China) Investment Limited so that Jia Yao WFOE would enter into contracts with suppliers of raw timber through Sino-Forest (China) Investment Limited, instead of authorized intermediaries.

With the successful establishment of Sino-Forest (China) Investment Limited and the subsequent establishment of Sino-Forest (Guangzhou) Trading Co. Ltd. and Sino-Forest (Suzhou) Trading Co. Ltd., we believe that we would have better opportunities to engage in trading activities through Sino-Forest (Guangzhou) Trading Co. Ltd. and Sino-Forest (Suzhou) Trading Co. *We anticipate that we will gradually phase out authorized intermediaries' involvement in these activities.* However, the pace of such a phase-out is not clear and we expect to continue to rely on the authorized intermediary in the sale of woods chips in the PRC for the foreseeable future.

[Emphasis added.]

100. Although it appeared that Sino transformed its business model over its history, from a producer and seller of wood chips to a seller of standing timber, in substance its overall business process did not change substantially. The most significant changes were the continual restructuring of Sino's organizational structure and its contractual arrangements with business partners and related entities. These changes were motivated, in whole or in part, by financial reporting objectives, specifically revenue recognition. Management consistently modified Sino's organizational structure and contractual arrangements to achieve revenue recognition at both greater values and at earlier points in time than is permissible under GAAP.

### **SINO'S CLASS PERIOD MISREPRESENTATIONS**

#### ***Sino's 2006 Results and AIF and its May 2007 Management Information Circular***

101. Prior to the opening of markets on March 19, 2007 (the first day of the Class Period), Sino issued and filed on SEDAR its 2006 Annual Consolidated Financial Statements and 2006 Annual MD&A. Each such document contained the Representation, which was false.

102. More particularly, Sino reported in each such document, on a GAAP basis, that its revenues and net income for the year ended December 31, 2006 were, respectively, US\$645.0 million and US\$111.6 million, and further reported, on a GAAP basis, that its assets as at

December 31, 2006 were US\$1.2 billion. According to these disclosure documents, Sino's revenues, net income and assets had increased from the prior year's results by, respectively, 31%, 36% and 35%. However, Sino's results for 2006, and its assets as at year-end 2006, were materially overstated.

103. Over the ten trading days following the issuance of Sino's inflated 2006 results, Sino's share price rose substantially on unusually heavy trading volume. At the close of trading on March 16, 2007 (the trading day prior to March 19, 2007), Sino's shares traded at \$10.10 per share. At the close of trading on March 29, 2007, Sino's shares traded at \$13.42 per share, which constituted an increase of approximately 33% from the March 19 closing price.

104. On March 30, 2007, Sino issued and filed on SEDAR its 2006 AIF. In that AIF, Sino stated:

...PRC laws and regulations require foreign companies to obtain licenses to engage in any business activities in the PRC. As a result of these requirements, we currently engage in our trading activities through PRC authorized intermediaries that have the requisite business licenses. There is no assurance that the PRC government will not take action to restrict our ability to engage in trading activities through our authorized intermediaries. ***In order to reduce our reliance on the authorized intermediaries, we intend to use a WFOE in the PRC to enter into contracts directly with suppliers of raw timber, and then process the raw timber, or engage others to process raw timber on its behalf, and sell logs, wood chips and wood-based products to customers, although it would not be able to engage in pure trading activities.***

[Emphasis added.]

105. In its 2007 AIF, which Sino filed on March 28, 2008, Sino again declared its intention to reduce its reliance upon AIs.

106. These statements were false and/or materially misleading when made, inasmuch as Sino had no intention to reduce materially its reliance on AIs, because its AIs were critical to Sino's

ability to inflate its revenue and net income. Rather, these statements had the effect of mitigating any investor concern arising from Sino's extensive reliance upon AIs.

107. Throughout the Class Period, Sino continued to depend heavily upon AIs for its purported sales of standing timber. Based in part upon management's provision for the amount the PRC tax authorities might seek to recover in relation to Sino's use of AIs, which provision increased over 400% from year-end 2006 to year-end 2010, it appears that Sino's reliance on AIs in fact *increased* during the Class Period.

108. On May 4, 2007, Sino issued and filed on SEDAR a Management Information Circular, and stated therein that "[m]aintaining a high standard of corporate governance is a top priority for the Board of Directors and the Corporation's management as both believe that effective corporate governance will help create and maintain shareholder value in the long term."

109. These statements were materially misleading when made, in that Chan and Poon, both of whom were then members of Sino's Board, had concealed from investors the Alkaner petition, their true qualifications to manage Sino, Sino's dealings with Leizhou, and that Sino's investment in SJXT was fictitious. The fact that Chan and Poon had knowingly concealed these facts from investors prior to the Class Period was material to persons who acquired Sino securities during the Class Period, because Chan and Poon were then in control of Sino, and their past misconduct demonstrated that they were unfit to manage Sino.

110. In any event, the failure to disclose these facts at any time during the Class Period rendered misleading Sino's declarations that a "high standard of corporate governance" was a "top priority."

***Sino's Class Period Misrepresentations in Relation to its AIs***

111. Throughout the Class Period, Sino materially understated the tax-related risks arising from its use of AIs.

112. Tax evasion penalties in the PRC are severe. Depending on whether the PRC authorities seek recovery of unpaid taxes by means of a civil or criminal proceeding, its claims for unpaid tax are subject to either a five- or ten-year limitation period. The unintentional failure to pay taxes is subject to a 18.75% per annum interest penalty, while an intentional failure to pay taxes is punishable with *unlimited* fines, depending on the severity of the infraction.<sup>2</sup>

113. Therefore, because Sino professed to be unable to determine whether its AIs have paid required taxes, the tax-related risks arising from Sino's use of AIs were potentially devastating. Sino failed, however, to disclose these aspects of the PRC tax regime in its Class Period disclosure documents, including and particularly in its discussions of its tax provisioning set forth in its Class Period financial statements and AIFs.

114. Based upon Sino's reported results, Sino's tax accruals in its 2007, 2008, 2009 and 2010 Audited Annual Financial Statements were materially deficient. Depending on whether the PRC tax authorities would assess interest at the rate of 18.75% per annum, or would assess no interest, on the unpaid income taxes of Sino's BVI subsidiaries, and depending also on whether one assumes that Sino's AIs have paid no income taxes or have paid 50% of the income taxes due to the PRC, then Sino's tax accruals as at year end 2007, 2008, 2009 and 2010 was understated by, respectively, US\$10 million to US\$150 million, US\$50 million to US\$260 million, US\$81 million to US\$371 million, and US\$83 million to US\$493 million. Importantly, were one to consider the impact of unpaid taxes other than unpaid income taxes (for example, unpaid value-

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<sup>2</sup> Prior to February 28, 2009, the latter penalty was capped at five times the unpaid taxes.

added taxes), then the amounts by which Sino's tax accruals were understated at year-end 2007, 2008, 2009 and 2010 would be substantially larger. The aforementioned estimates of the amounts by which Sino's tax accruals were understated also assume that the PRC tax authorities only impose interest charges on Sino's BVI Subsidiaries and impose no other penalties for unpaid taxes, and assume further that the PRC authorities seek back taxes only for the preceding five years. As indicated above, each of these assumptions is likely to be unduly optimistic. In any case, Sino's inadequate tax accruals violated GAAP.

115. Sino also violated GAAP in its 2009 Audited Annual Financial Statements by failing to apply to its 2009 financial results the PRC tax guidance that was issued in February 2010. Although that guidance was issued after year-end 2009, GAAP required that Sino apply that guidance to its 2009 financial results, because that guidance was issued in the subsequent events period.

116. Based upon Sino's reported profit margins on its dealings with AIs, which margins are extraordinary both in relation to the profit margins of Sino's peers, and in relation to the limited risks that Sino purports to assume in its transactions with its AIs, Sino's AIs are not satisfying their tax obligations, a fact that was either known to the Defendants or ought to have been known. If Sino's extraordinary profit margins are real, then Sino and its AIs must be dividing the gains from non-payment of taxes to the PRC.

117. During the Class Period, Sino also failed to disclose the risks relating to the repatriation of its earnings from the PRC. In 2010, Sino added two new sections to its AIF regarding the risk that it would not be able to repatriate earnings from its BVI subsidiaries (which deal with the AIs). The amount of retained earnings that may not be able to be repatriated is stated therein to be US\$1.4 billion. Notwithstanding this disclosure, Sino did not disclose that it would be unable

to repatriate *any* earnings absent proof of payment of PRC taxes, which it has admitted that it lacks.

118. In addition, there are material discrepancies in Sino's descriptions of its accounting treatment of its AIs. Beginning in the 2003 AIF, Sino described its AIs as follows:

Because of the provisions in the Operational Procedures that specify when we and the authorized intermediary assume the risks and obligations relating to the raw timber or wood chips, as the case may be, we treat these transactions for accounting purposes as providing that we take title to the raw timber when it is delivered to the authorized intermediary. Title then passes to the authorized intermediary once the timber is processed into wood chips. ***Accordingly, we treat the authorized intermediaries for accounting purposes as being both our suppliers and customers in these transactions.***

[Emphasis added.]

119. Sino's disclosures were consistent in that regard up to and including Sino's first AIF issued in the Class Period, which states:

Because of the provisions in the Operational Procedures that specify when we and the AI assume the risks and obligations relating to the raw timber or wood chips, as the case may be, we treat these transactions for accounting purposes as providing that we take title to the raw timber when it is delivered to the AI. Title then passes to the AI once the timber is processed into wood chips. ***Accordingly, we treat the AI for accounting purposes as being both our supplier and customer in these transactions.***

[Emphasis added.]

120. In subsequent AIFs, Sino ceased without explanation to disclose whether it treated AIs for accounting purposes as being both the supplier and the customer.

121. Following the issuance of Muddy Waters' report on the last day of the Class Period, however, Sino declared publicly that Muddy Waters was "wrong" in its assertion that, for accounting purposes, Sino treated its AIs as being both supplier and customer in transactions. This claim by Sino implies either that Sino misrepresented its accounting treatment of AIs in its

2006 AIF (and in its AIFs for prior years), or that Sino changed its accounting treatment of its AIs after the issuance of its 2006 AIF. If the latter is true, then Sino was obliged by GAAP to disclose its change in its accounting treatment of its AIs. It failed to do so.

***Sino Overstates its Yunnan Forestry Assets***

122. In a press release issued by Sino and filed on SEDAR on March 23, 2007, Sino announced that it had entered into an agreement to sell 26 million shares to several institutional investors for gross proceeds of US\$200 million, and that the proceeds would be used for the acquisition of standing timber, including pursuant to a new agreement to purchase standing timber in Yunnan Province. It further stated in that press release that Sino-Panel (Asia) Inc. (“Sino-Panel”), a wholly-owned subsidiary of Sino, had entered on that same day into an agreement with Gengma Dai and Wa Tribes Autonomous Region Forestry Company Ltd., (“Gengma Forestry”) established in Lincang City, Yunnan Province in the PRC, and that, under that Agreement, Sino-Panel would acquire approximately 200,000 hectares of non-state owned commercial standing timber in Lincang City and surrounding cities in Yunnan for US\$700 million to US\$1.4 billion over a 10-year period.

123. These same terms of Sino’s Agreement with Gengma Forestry were disclosed in Sino’s Q1 2007 MD&A. Moreover, throughout the Class Period, Sino discussed its purported Yunnan acquisitions in the Impugned Documents, and Pöyry repeatedly made statements regarding said holdings, as particularized below.

124. However, the reported acquisitions did not take place. As the *Globe* later revealed, Sino “substantially overstated the size and value of its forestry holdings in China’s Yunnan Province, according to figures provided by senior forestry officials and a key business partner there.” Sino simply does not own the trees it claims to own in Yunnan.

***Sino Overstates its Suriname Forestry Assets***

125. In mid-2010, Sino became a majority shareholder of Greenheart Group Ltd., a Bermuda corporation having its headquarters in Hong Kong and a listing on the Hong Kong Stock Exchange (“Greenheart”).

126. In August 2010, Greenheart issued an aggregate principal amount of US\$25,000,000 convertible notes for gross proceeds of US\$24,750,000. The sole subscriber of these convertible notes was Greater Sino Holdings Limited, an entity in which Murray has an indirect interest. In addition, Chan and Murray then became members of Greenheart’s Board, Chan became the Board’s Chairman, and Martin became the CEO of Greenheart and a member of its Board.

127. On August 24, 2010 and December 28, 2010, Greenheart granted to Chan, Martin and Murray options to purchase, respectively, approximately 6.8 million, 6.8 million and 1.1 million Greenheart shares. The options are exercisable for a five-year term.

128. As at March 31, 2011, General Enterprise Management Services International Limited, a company in which Murray has an indirect interest, held 7,000,000 shares of Greenheart, being 0.9% of the total issued and outstanding shares of Greenheart.

129. As a result of the aforesaid transactions and interests, Sino, Chan, Martin and Murray stood to profit handsomely from any inflation in the market price of Greenheart’s shares.

130. At all material times, Greenheart purported to have forestry assets in New Zealand and Suriname. On March 1, 2011, Greenheart issued a press release in which it announced that:

**Greenheart acquires certain rights to additional 128,000 hectare concession in Suriname**

\*\*\*\*\*

**312,000 hectares now under Greenheart management**



Hong Kong, March 1, 2011 – Greenheart Group Limited (“Greenheart” or “the Company”) (HKSE: 00094), an investment holding company with forestry assets in Suriname and New Zealand (subject to certain closing conditions) today announced that *the Company has acquired 60% of Vista Marine Services N.V. (“Vista”), a private company based in Suriname, South America that controls certain harvesting rights to a 128,000 hectares hardwood concession. Vista will be rebranded as part of the Greenheart Group. This transaction will increase Greenheart’s concessions under management in Suriname to approximately 312,000 hectares.* The cost of this acquisition is not material to the Company as a whole but the Company is optimistic about the prospects of Vista and the positive impact that it will bring. *The concession is located in the Sipalawini district of Suriname, South America, bordering Lake Brokopondo and has an estimated annual allowable cut of approximately 100,000 cubic meters.*

Mr. Judson Martin, Chief Executive Officer of Greenheart and Vice-Chairman of Sino-Forest Corporation, the Company’s controlling shareholder said, “This acquisition is in line with our growth strategy to expand our footprint in Suriname. In addition to increased harvestable area, this acquisition will bring synergies in sales, marketing, administration, financial reporting and control, logistics and overall management. *I am pleased to welcome Mr. Ty Wilkinson to Greenheart as our minority partner. Mr. Wilkinson shares our respect for the people of Suriname and the land and will be appointed Chief Executive Officer of this joint venture and be responsible for operating in a sustainable and responsible manner.* This acquisition further advances Greenheart’s strategy of becoming a global agri-forestry company. We will continue to actively seek well-priced and sustainable concessions in Suriname and neighboring regions in the coming months.”

#### About Ty Wilkinson

*Mr. Wilkinson has over twenty years of experience in the agricultural and forestry business. He was awarded the prestigious “Farmer and Rancher of the year” award in the USA, in recognition of his work on water conservation, perfecting the commercial use of drip irrigation and maximizing crop yield through the use of technical soil research and analysis. Mr. Wilkinson also has extensive knowledge in sustainable forestry management, forestry planning, infrastructure development, harvest schedules, lumber drying, lumber processing, extensive local knowledge as well as regional business networks. He has been living in Suriname since 2001.*

[Emphasis added.]

131. In its 2010 AIF, filed on SEDAR on March 31, 2011, Sino stated:

We hold a majority interest in Greenheart Group which, together with its subsidiaries, owns certain rights and *manages approximately 312,000 hectares of hardwood forest concessions in the Republic of Suriname, South America* (“Suriname”) and 11,000 hectares of a radiata pine plantation on 13,000 hectares of freehold land in New Zealand as at March 31, 2011. *We believe that our ownership in Greenheart Group will*

***strengthen our global sourcing network in supplying wood fibre for China in a sustainable and responsible manner.***

[Emphasis added.]

132. In its Annual Report for 2010, which Sino filed on SEDAR on May 10, 2011, Martin stated:

I am honored to report to you for the first time as Vice Chairman of Sino-Forest and Chief Executive Officer of Greenheart Group.

[...]

Greenheart's strategy is to be Sino-Forest's international growth vehicle for acquiring sustainable and profitable forestry assets located outside China to serve the growing wood deficit within China while at the same time maintaining the ability to manage and operate in other markets around the world. At the end of 2010, Greenheart had three primary assets; a 60% interest in a 184,000 hectare hardwood concession located in western Suriname (Sino-Forest currently owns the remaining 40% minority interest); a commitment to acquire 13,000 hectares of freehold land including 11,000 hectares of softwood radiata pine plantations in New Zealand (which was completed subsequent to year end); and US\$78 million in cash.

***In the first quarter of 2011, we acquired 60% of Vista Marine Services N.V., which holds certain harvesting rights to a 128,000-hectare concession in eastern Suriname. This acquisition expands Greenheart's land under management in Suriname to approximately 312,000 hectare. We are currently building two large-scale wood processing facilities, which we expect to complete late this year, which will allow us to process logs into lumber and other value-added products such as flooring, decking and special millwork.***

***Greenheart's strategy in Suriname is to continue to expand our concession footprint and be the leader in the sustainable timber industry. We are committed to low-impact harvesting and silviculture methods as prescribed by Suriname's Centre for Agricultural Research ("CELOS"), and we will be working towards Forest Stewardship Council ("FSC") certification in all our operations. The responsible care of people and the environment is our corporate policy but also our state of mind.***

[Emphasis added.]

133. The foregoing statements were false and/or materially misleading when made, for the reasons set out in paragraphs 135 to 138 below.

134. Shortly before Greenheart's purported acquisition of Vista Marine Services N.V. ("Vista"), Vista was founded by Ty Wilkinson, an American citizen who formerly resided in Sarasota, Florida. Although Greenheart saw fit to disclose in its March 1, 2011 press release that Mr. Wilkinson, Greenheart's new Suriname CEO, was once named "Farmer and Rancher of the year," Greenheart failed to disclose that the Circuit Court of Sarasota County, Florida, had issued a warrant for Mr. Wilkinson's arrest in October 2009, and that Mr. Wilkinson abandoned residence in the United States at least in part to avoid arrest, and also to avoid paying various debts Wilkinson owes to a former business associate and others.

135. There is no record of Greenheart in the Suriname Trade Register maintained by the Chamber of Commerce in Suriname, nor is there any record of Greenheart with the Suriname Foundation for Forest Management and Production Control.

136. In addition, under the Suriname *Forest Management Act*, it is prohibited for one company or a group of companies in which one person or company has a majority interest to control more than 150,000 hectares of land under concession.

137. Finally, Vista's forestry concessions are located in a region of Suriname populated by the Saramaka, an indigenous people. Pursuant to the American Convention on Human Rights and a decision of the Inter-American Court of Human Rights, the Saramaka people must have effective control over their land, including the management of their reserves, and must be effectively consulted by the State of Suriname. Neither Sino nor Greenheart has disclosed that Vista's purported concessions in Suriname, if they exist at all, are impaired due to the unfulfilled rights of the indigenous peoples of Suriname.

***Jiangxi Forestry Assets***

138. On June 11, 2009, Sino issued a press release in which it stated:

Sino-Forest Corporation (TSX: TRE), a leading commercial forest plantation operator in China, announced today that its wholly-owned subsidiary, Sino-Panel (China) Investments Limited (“Sino-Panel”), has entered into a Master Agreement for the Purchase of Pine and Chinese Fir Plantation Forests (the “Jiangxi Master Agreement”) with Jiangxi Zhonggan Industrial Development Company Limited (“Jiangxi Zhonggan”), which will act as the authorized agent for the original plantation rights holders.

Under the Jiangxi Master Agreement, Sino-Panel will, through PRC subsidiaries of Sino-Forest, acquire between 15 million and 18 million cubic metres (m<sup>3</sup>) of wood fibre located in plantations in Jiangxi Province over a three-year period with a price not to exceed RMB300 per m<sup>3</sup>, to the extent permitted under the relevant PRC laws and regulations. ***The plantations in which such amount of wood fibre to acquire is between 150,000 and 300,000 hectares*** to achieve an estimated average wood fibre yield of approximately 100 m<sup>3</sup> per hectare, and include tree species such as pine, Chinese fir and others. Jiangxi Zhonggan will ensure plantation forests sold to Sino-Panel and its PRC subsidiaries are non-state-owned, non-natural, commercial plantation forest trees.

In addition to securing the maximum tree acquisition price, Sino-Panel has pre-emptive rights to lease the underlying plantation land at a price, permitted under the relevant PRC laws and regulations, not to exceed RMB450 per hectare per annum for 30 years from the time of harvest. The land lease can also be extended to 50 years as permitted under PRC laws and regulations. The specific terms and conditions of purchasing or leasing are to be determined upon the execution of definitive agreements between the PRC subsidiaries of Sino-Panel and Jiangxi Zhonggan upon the authorisation of original plantation rights holders, and subject to the requisite governmental approval and in compliance with the relevant PRC laws and regulations.

***Sino-Forest Chairman and CEO Allen Chan said, “We are fortunate to have been able to capture and support investment opportunities in China’s developing forestry sector by locking up a large amount of fibre at competitive prices. The Jiangxi Master Agreement is Sino-Forest’s fifth, long-term, fibre purchase agreement during the past two years. These five agreements cover a total plantation area of over one million hectares in five of China’s most densely forested provinces.”***

[Emphasis added.]

139. According to Sino’s 2010 Annual MD&A, as of December 31, 2010, Sino had acquired 59,700 ha of plantation trees from Jiangxi Zhonggan Industrial Development Company Limited (“Zhonggan”) for US\$269.1 million under the terms of the master agreement. (In its interim report for the second quarter of 2011, which was issued after the Class Period, Sino claims that, as at June 30, 2011, this number had increased to 69,100 ha, for a purchase price of US\$309.6 million).

140. However, as was known to Sino, Chan, Poon and Horsley, and as ought to have been known to the remaining Individual Defendants, E&Y and Pöyry, Sino's plantation acquisitions through Zhonggan are far smaller than Sino has claimed.

141. In August 2011, a supervisor of the Forestry Bureau of Nanchang, the capitol of Jiangxi Province, affirmed that he had never heard of Zhonggan. In that same month, the Jiangxi Forestry Bureau, which has jurisdiction over the Province of Jiangxi, was able to confirm only that Zhonggan had rented the land use rights of 3,333 ha from local farmers.

142. Zhonggan's offices belie the purported scope and nature of Zhonggan's business. During a visit to Zhonggan's offices in August 2011, no personnel were present during business hours, there was no signage outside the office, and there was a CCTV camera and a fingerprint entry machine installed near the office entrance.

143. Zhonggan was formed in January 2008, only 18 months before agreeing to sell to Sino's subsidiary up to 300,000 ha of plantation forest. Moreover, when it was established, Zhonggan was capitalized with a mere ¥5 million.

144. Irrespective of the true extent of Zhonggan's transactions in Jiangxi forestry plantations, Sino failed to disclose, in violation of GAAP, that Zhonggan was a related party of Sino. More particularly, according to AIC records, the legal representative of Zhonggan is Lam Hong Chiu, who is an executive vice president of Sino. Lam Hong Chiu is also a director and a 50% shareholder of China Square Industrial Limited, a BVI corporation which, according to AIC records, owns 80% of the equity of Zhonggan.

***Misrepresentations Regarding Related Parties other than Zhonggan***

145. On January 12, 2010, Sino issued a press release in which it announced: the acquisition by one of its wholly-owned subsidiaries of Homix Limited ("Homix"), which it described as a

company engaged in research and development and manufacturing of engineered-wood products in China, for an aggregate amount of US\$7.1 million. That press release stated:

HOMIX has an R&D laboratory and two engineered-wood production operations based in Guangzhou and Jiangsu Provinces, covering eastern and southern China wood product markets. The company has developed a number of new technologies with patent rights, specifically suitable for domestic plantation logs including poplar and eucalyptus species. HOMIX specializes in curing, drying and dyeing methods for engineered wood and has the know-how to produce recomposed wood products and laminated veneer lumber. Recomposed wood technology is considered to be environment-friendly and versatile as it uses fibre from forest plantations, recycled wood and/or wood residue. This reduces the traditional use of large-diameter trees from natural forests. There is growing demand for recomposed wood technology as it reduces cost for raw material while increases the utilization and sustainable use of plantation fibre for the production of furniture and interior/exterior building materials.

[...]

Mr. Allen Chan, Sino-Forest's Chairman & CEO, said, "As we continue to ramp up our replanting programme with improved eucalyptus species, it is important for Sino-Forest to continue investing in the research and development that maximizes all aspects of the forest product supply chain. Modernization and improved productivity of the wood processing industry in China is also necessary given the country's chronic wood fibre deficit. Increased use of technology improves operation efficiency, and maximizes and broadens the use of domestic plantation wood, which reduces the need for logging domestic natural forests and for importing logs from strained tropical forests. HOMIX has significant technological capabilities in engineered-wood processing."

Mr. Chan added, "By acquiring HOMIX, we intend to use six-year eucalyptus fibre instead of 30-year tree fibre from other species to produce quality lumber using recomposed technology. We believe that this will help preserve natural forests as well as improve the demand for and pricing of our planted eucalyptus trees."

146. Sino's 2009 Annual Audited Financial Statements, Q1/2010 Unaudited Interim Financial Statements, 2010 Annual Audited Financial Statements, the MD&As related to each of the aforementioned financial statements, and Sino's AIFs for 2009 and 2010, each discussed the acquisition of Homix, but nowhere disclosed that Homix was in fact a party related to Sino.

147. More particularly, Hua Chen, a Senior Vice President, Administration & Finance, of Sino in the PRC, and who joined Sino in 2002, is a 30% shareholder of an operating subsidiary of Homix, Jiangsu Dayang Wood Co., Ltd.

148. Pursuant to GAAP, Sino was required to provide, among other things, a description of the relationship between the transacting parties when dealing with related parties. GAAP recognizes that detail on related party transactions is crucial: “Information about related party transactions is often of more significance to a financial statement user than information about unrelated party transactions, regardless of the size of such transactions.”

149. Thus, Sino’s failure to disclose that Homix was a related party was a violation of GAAP, and a misrepresentation.

150. Finally, Homix has no patent designs registered with the PRC State Intellectual Property Office, a fact also not disclosed by Sino at the time of the Homix acquisition or subsequently.

#### ***Misrepresentations Regarding Sales of Standing Timber***

151. Every financial statement and MD&A issued during the Class Period overstates Sino’s sales of standing timber to a material degree, and overstates to a material degree Sino’s reported revenues and net income for the period in question.

152. Throughout the Class Period, Sino purported to sell “standing timber.” As particularized above, such sales did not occur, or did not occur in a manner such that revenue could be recorded pursuant to GAAP.

#### ***Misrepresentations Regarding Purchases of Forestry Assets***

153. As particularized above, Sino overstated its acquisition of forestry assets in Yunnan and Jiangxi Provinces in the PRC and in Suriname. Accordingly, Sino’s total assets are overstated to

a material degree in the Impugned Documents in violation of GAAP, and each such statement of Sino's total assets constitutes a misrepresentation.

154. In addition, during the Class Period, Pöyry and entities affiliated with it made statements that are misrepresentations in regard to Sino's Yunnan Province "assets," namely:

- (a) In a report dated March 15, 2008, filed on SEDAR on March 31, 2008. Pöyry: (a) stated that it had determined the valuation of the Sino forest assets to be US\$3.2 billion as at 31 December 2007; (b) provided tables and figures regarding Yunnan; (c) stated that "Stands in Yunnan range from 20 ha to 1000 ha," that "In 2007 Sino-Forest purchased an area of mixed broadleaf forest in Yunnan Province," that "Broadleaf forests already acquired in Yunnan are all mature," and that "Sino-Forest is embarking on a series of forest acquisitions/expansion efforts in Hunan, Yunnan and Guangxi;" and (d) provided a detailed discussion of Sino's Yunnan "holdings" at Appendixes 3 and 5;
- (b) In a report dated April 1, 2009 and filed on SEDAR on April 2, 2009, Pöyry stated that "[t]he area of forest owned in Yunnan has quadrupled from around 10 000 ha to almost 40 000 ha over the past year," provided figures and tables regarding Yunnan, and stated that "Sino-Forest has increased its holding of broadleaf crops in Yunnan during 2008, with this province containing nearly 99% of its broadleaf resource;"
- (c) In a "Final Report" dated April 23, 2010, filed on SEDAR on April 30, 2010 Pöyry stated that "Guangxi, Hunan and Yunnan are the three largest provinces in terms of Sino-Forest's holdings. The largest change in area by province, both in absolute and relative terms [sic] has been Yunnan, where the area of forest owned has almost tripled, from around 39 000 ha to almost 106 000 ha over the past year," provided figures and tables regarding Yunnan, stated that "Yunnan contains 106 000 ha, including 85 000 ha or 99% of the total broadleaf forest," stated that "the three provinces of Guangxi, Hunan and Yunnan together contain 391 000 ha or about 80% of the total forest area of 491 000 ha" and that "[a]lmost



97% of the broadleaf forest is in Yunnan,” and provided a detailed discussion of Sino’s Yunnan “holdings” at Appendixes 3 and 4;

- (d) In a “Summary Valuation Report” regarding “Valuation of Purchased Forest Crops as at 31 December 2010” and dated May 27, 2011, Pöyry provided tables and figures regarding Yunnan, stated that “[t]he major changes in area by species from December 2009 to 2010 has been in Yunnan pine, with acquisitions in Yunnan and Sichuan provinces” and that “[a]nalysis of [Sino’s] inventory data for broadleaf forest in Yunnan, and comparisons with an inventory that Pöyry undertook there in 2008 supported the upwards revision of prices applied to the Yunnan broadleaf large size log,” and stated that “[t]he yield table for Yunnan pine in Yunnan and Sichuan provinces was derived from data collected in this species in these provinces by Pöyry during other work;” and
- (e) In a press release titled “Summary of Sino-Forest’s China Forest Asset 2010 Valuation Reports” and which was “jointly prepared by Sino-Forest and Pöyry to highlight key findings and outcomes from the 2010 valuation reports,” Pöyry reported on Sino’s “holdings” and estimated the market value of Sino’s forest assets on the 754,816 ha to be approximately US\$3.1 billion as at December 31, 2010.

155. Statements made by Pöyry regarding the value of Sino’s forestry “assets” that were misrepresentations were incorporated, with Pöyry’s consent, into the 2007 Annual MD&A, the Amended 2007 Annual MD&A, each of the 2008 Q1, Q2, Q3, Annual and amended Annual MD&As, each of the 2009 Q1, Q2, Q3 and Annual MD&As, and each of the 2010 Q1, Q2 and Q3 MD&As.

***Misrepresentations Regarding the Failure to Disclose Sino's True History***

156. In the Prospectuses, Sino described its history, but did not disclose the Alkaner petition, the true qualifications of Poon and Chan, that the SJXT investment was fictitious, or that the revenues generated by Leizhou were overstated.

157. In particular, the June 2007 Prospectus stated merely that:

The Corporation was formed under the *Business Corporations Act* (Ontario) upon the amalgamation of Mt. Kearsarge Minerals Inc. and 1028412 Ontario Inc. pursuant to articles of amalgamation dated March 14, 1994. The articles of amalgamation were amended by articles of amendment filed on July 20, 1995 and May 20, 1999 to effect certain changes in the provisions attaching to the Corporation's class A subordinate-voting shares and class B multiple-voting shares. On June 25, 2002, the Corporation filed articles of continuance to continue under the *Canada Business Corporations Act*. On June 22, 2004, the Corporation filed articles of amendment whereby its class A subordinate-voting shares were reclassified as Common Shares and its class B multiple-voting shares were eliminated.

158. Similarly, the June 2009 Prospectus stated only that:

The Corporation was formed under the *Business Corporations Act* (Ontario) upon the amalgamation of Mt. Kearsarge Minerals Inc. and 1028412 Ontario Inc. pursuant to articles of amalgamation dated March 14, 1994. The articles of amalgamation were amended by articles of amendment filed on July 20, 1995 and May 20, 1999 to effect certain changes in the provisions attaching to the Corporation's class A subordinate-voting shares and class B multiple-voting shares. On June 25, 2002, the Corporation filed articles of continuance to continue under the *Canada Business Corporations Act*. On June 22, 2004, the Corporation filed articles of amendment whereby its class A subordinate-voting shares were reclassified as Common Shares and its class B multiple-voting shares were eliminated.

159. Finally, the December 2009 Prospectus stated only that:

The Corporation was formed under the *Business Corporations Act* (Ontario) upon the amalgamation of Mt. Kearsarge Minerals Inc. and 1028412 Ontario Inc. pursuant to articles of amalgamation dated March 14, 1994. The articles of amalgamation were amended by articles of amendment filed on July 20, 1995 and May 20, 1999 to effect certain changes in the provisions attaching to the Corporation's class A subordinate-voting shares and class B multiple-voting shares. On June 25, 2002, the Corporation filed articles of continuance to continue under the *Canada Business Corporations Act* (the "CBCA"). On June 22, 2004,

the Corporation filed articles of amendment whereby its class A subordinate-voting shares were reclassified as Common Shares and its class B multiple-voting shares were eliminated.

160. The failure to disclose the Alkaner petition, Chan's and Poon's true qualifications, and the true nature of and revenues from Sino's SJXT and Leizhou investments in the historical narrative in the Prospectuses rendered those Prospectuses false and misleading, inasmuch as those historical facts would have alerted persons who purchased Sino shares under the Prospectuses to the highly elevated risk of investing in an issuer that was managed by Poon and Chan.

***Misrepresentations Regarding Sino's Margins and Taxes***

161. Sino never disclosed the true source of its elevated profit margins and the true nature of the tax-related risks to which it was exposed, as particularized above. This omission rendered each of the following statements a misrepresentation:

- (a) In the 2006 Annual Financial Statements, note 11 [b] "Provision for tax related liabilities" and associated text;
- (b) In the 2006 Annual MD&A, the subsection "Provision for Tax Related Liabilities" in the section "Critical Accounting Estimates," and associated text;
- (c) In the AIF dated March 30, 2007, the section "Estimation of the Company's provision for income and related taxes," and associated text;
- (d) In the Q1 and Q2 2007 Financial Statements, note 5 "Provision for Tax Related Liabilities," and associated text;
- (e) In the Q3 2007 Financial Statements, note 6 "Provision for Tax Related Liabilities," and associated text;
- (f) In the 2007 Annual Financial Statements, note 13 [b] "Provision for tax related liabilities," and associated text;

- (g) In the 2007 Annual MD&A and Amended 2007 Annual MD&A, the subsection “Provision for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text;
- (h) In the AIF dated March 28, 2008, the section “Estimation of the Corporation’s provision for income and related taxes,” and associated text;
- (i) In the Q1, Q2 and Q3 2008 Financial Statements, note 12 “Provision for Tax Related Liabilities,” and associated text;
- (j) In the Q1, Q2 and Q3 2008 MD&As, the subsection “Provision for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text;
- (k) In the 2008 Annual Financial Statements, note 13 [d] “Provision for tax related liabilities,” and associated text;
- (l) In the 2008 Annual MD&A and Amended 2008 Annual MD&A, the subsection “Provision for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text;
- (m) In the AIF dated March 31, 2009, the section “We may be liable for income and related taxes to our business and operations, particularly our BVI Subsidiaries, in amounts greater than the amounts we have estimated and for which we have provisioned,” and associated text;
- (n) In the Q1, Q2 and Q3 2009 Financial Statements, note 13 “Provision for Tax Related Liabilities,” and associated text;
- (o) In the Q1, Q2 and Q3 2009 MD&As, the subsection “Provision for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text;
- (p) In the 2009 Annual Financial Statements, note 15 [d] “Provision for tax related liabilities,” and associated text;

- (q) In the 2009 Annual MD&A, the subsection “Provision for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text;
- (r) In the AIF dated March 31, 2010, the section “We may be liable for income and related taxes to our business and operations, particularly our BVI Subsidiaries, in amounts greater than the amounts we have estimated and for which we have provisioned,” and associated text;
- (s) In the Q1 and Q2 2010 Financial Statements, note 14 “Provision for Tax Related Liabilities,” and associated text;
- (t) In the Q1 and Q2 2010 MD&As, the subsection “Provision for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text;
- (u) In the Q3 2010 Financial Statements, note 14 “Provision and Contingencies for Tax Related Liabilities,” and associated text; and
- (v) In the Q3 2010 MD&As, the subsection “Provision and Contingencies for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text;
- (w) In the 2010 Annual Financial Statements, note 18 “Provision and Contingencies for Tax Related Liabilities,” and associated text;
- (x) In the 2010 Annual MD&A, the subsection “Provision and Contingencies for Tax Related Liabilities” in the section “Critical Accounting Estimates,” and associated text; and
- (y) In the AIF dated March 31, 2011, the section “We may be liable for income and related taxes to our business and operations, particularly our BVI Subsidiaries, in amounts greater than the amounts we have estimated and for which we have provisioned,” and associated text.

162. In every Impugned Document that is a financial statement, the line item “Accounts payable and accrued liabilities” and associated figures on the Consolidated Balance Sheets fails to properly account for Sino’s tax accruals and is a misrepresentation.

#### **CHAN AND HORSLEY’S FALSE CERTIFICATIONS**

163. Pursuant to National Instrument 52-109, the defendants Chan, as CEO, and Horsley, as CFO, were required at the material times to certify Sino’s annual and quarterly MD&As and Financial Statements as well as the AIFs (and all documents incorporated into the AIFs). Such certifications included statements that the filings “do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made” and that the reports “fairly present in all material respects the financial condition, results of operations and cash flows of the issuer.”

164. As particularized elsewhere herein, however, the Impugned Documents contained the Representation, which was false, as well as the other misrepresentations alleged above. Accordingly, the certifications given by Chan and Horsley were false and were themselves misrepresentations. Chan and Horsley made such false certifications knowingly or, at a minimum, recklessly.

#### **THE TRUTH IS REVEALED**

165. On June 2, 2011, Muddy Waters issued its initial report on Sino, and stated in part therein:

Sino-Forest Corp (TSE: TRE) is the granddaddy of China RTO frauds. It has always been a fraud – reporting excellent results from one of its early joint ventures – even though, because of TRE’s default on its investment obligations, the JV never went into operation. TRE just lied.

The foundation of TRE's fraud is a convoluted structure whereby it claims to run most of its revenues through "authorized intermediaries" ("AI"). AIs are supposedly timber trader customers who purportedly pay much of TRE's value added and income taxes. At the same time, these AIs allow TRE a gross margin of 55% on standing timber merely for TRE having speculated on trees.

The sole purpose of this structure is to fabricate sales transactions while having an excuse for not having the VAT invoices that are the mainstay of China audit work. If TRE really were processing over one billion dollars in sales through AIs, TRE and the AIs would be in serious legal trouble. No legitimate public company would take such risks – particularly because this structure has zero upside.

[...]

On the other side of the books, TRE massively exaggerates its assets. TRE significantly falsifies its investments in plantation fiber (trees). It purports to have purchased \$2.891 billion in standing timber under master agreements since 2006 [...]

[...]

#### Valuation

Because TRE has \$2.1 billion in debt outstanding, which we believe exceeds the potential recovery, we value its equity at less than \$1.00 per share.

166. Muddy Waters also disclosed in its initial report that Sino had failed to disclose various related party transactions, including its dealings with Jiangxi Zhonggan Industrial Development Company Ltd.

167. After Muddy Waters' initial report became public, Sino shares fell to \$14.46, at which point trading was halted (a decline of 20.6% from the pre-disclosure close of \$18.21). When trading was allowed to resume the next day, Sino's shares fell to a close of \$5.23 (a decline of 71.3% from June 1).

168. On June 3, 2011, Sino announced the formation of an "Independent Committee," comprised of Ardell (Chair), Bowland and Hyde, to investigate Muddy Waters' allegations and report to Sino's Board in that regard.

169. However, due in part to the fact that Bowland and Hyde are former E&Y personnel, they are not independent, particularly for purposes of investigating E&Y's failure to audit Sino properly.

170. On June 14, Sino issued its Q1 2011 Financial Statements. Those financial statements contained the following notice:

**Notice of no auditor review of the condensed interim consolidated financial statements.**

The accompanying unaudited condensed interim consolidated financial statements (the "Interim Financial Statements") have not been reviewed by the Company's external auditors.

On June 2, 2011, Muddy Waters, LLC issued a report (the "Report") containing various allegations regarding the Company, its assets, operations and financial results. As a result of such report, on June 2, 2011, the Board of Directors of the Company appointed a committee of independent directors (the "Independent Committee") to thoroughly examine and review the allegations contained in the Report, and report back to the Board of Directors. The Independent Committee has retained independent legal counsel in Canada, Hong Kong and China as well as independent accounting firm Pricewaterhouse Coopers LLP to assist with the examination.

The Company's external auditors were initially engaged to conduct a review of the accompanying Interim Financial Statements in accordance with Canadian standards for the auditor review of interim financial statements. The Company's auditors have advised that they are unable to complete a review of these financial statements until the completion of the examination and review by the Independent Committee and the auditors' consideration of the results thereof.

The Board of Directors and management believe that, based on information currently available to them, the Interim Financial Statements were compiled in accordance with International Financial Reporting Standards ("IFRS") and fairly depict the financial condition and results of operations of the Company. However, in the event that the allegations set forth in the Report prove to be accurate, in whole or in part, the information set forth in the Interim Financial Statements may differ materially and the Interim Financial Statements could be subject to restatement. As a result, readers should exercise caution in reviewing such financial statements. See Note 2.1 of the Interim Financial Statements.



171. That same day, Sino held its Q1 2011 Earnings Call. On that call, Ardell stated that “particular reference was made to a number of the directors that this is an opportunity for them to be in and buying significant amounts of shares to demonstrate strong belief in the company. ***And I can assure you that if we had the choice, we certainly would at this stage***” (emphasis added). Ardell thereby confirmed that he had prejudged the outcome of his committee’s investigation, and that his committee was not independent.

172. On Saturday June 18 and Sunday June 19, 2011, the *Globe* published an in-depth investigative report on Sino.

173. The June 18 article, titled “Key partner casts doubt on Sino-Forest claim,” read, in material part:

Embattled Sino-Forest Corp., once Canada’s biggest publicly-traded timber company, appears to have substantially overstated the size and value of its forestry holdings in China’s Yunnan province, according to figures provided by senior forestry officials and a key business partner there.

During two weeks of on-the-ground reporting that included interviews with Chinese government officials, forestry experts, local business operators and brokers, The Globe and Mail uncovered a number of glaring inconsistencies that raise doubts about the company’s public statements regarding the value of the assets that lie at the centre of the company’s core business of buying and selling Chinese timber rights.

[...]

The Globe’s investigation raises particularly hard questions about a key agreement in March, 2007, that Sino-Forest says gave it the right to buy timber rights for up to 200,000 hectares of forest in Yunnan over a 10-year period for between \$700-million (U.S.) and \$1.4-billion. The trees were to be bought through a series of agreements with an entity called Gengma Dai and Wa Tribes Autonomous Region Forestry Co. Ltd., also known as Gengma Forestry.

The company says it has fulfilled virtually all of the agreement with Gengma and now owns more than 200,000 hectares in Yunnan.

But officials with Gengma Forestry, including the chairman, dispute the company's account of the deal, telling *The Globe and Mail* that the actual numbers are much smaller.

Xie Hongting, the chairman of Gengma Forestry, said in an interview that the transactions carried out so far by Sino-Forest amounted to less than 14,000 hectares.

Asked how many deals Gengma had conducted with Sino-Forest, Mr. Xie said: "I've told you that we sold them almost 200,000 mu." (Mu is a Chinese unit of land measurement; 15 mu equals one hectare.)

Mr. Xie's account corroborates the assertions of senior forestry officials in the province. Speaking on condition of anonymity, these officials challenged the company's statements that it controls more than 200,000 hectares of Yunnan trees, and said they are now investigating.

[...]

While Gengma Forestry officials question Sino-Forest's account of the 2007 deal, local land brokers said it would be difficult to find 200,000 hectares of quality land leases to complete that agreement.

[...]

Senior forestry officials in the province challenged the company's assertion that it controls about 200,000 hectares of forest in the region. Speaking on condition they not be identified, they said their records showed Sino-Forest manages far less than that and said the Yunnan Forestry Bureau would begin an investigation aimed at determining the company's true holdings.

In addition to the questions about Sino-Forest's disclosures on the size of its holdings, forestry officials, as well as local timber brokers who spoke to *The Globe* raised questions regarding the value Sino-Forest attributes to its Yunnan assets.

"It's very hard for anyone to say what the value of their property is," said one forestry official, adding that forested land in Yunnan needed to be evaluated by a special body jointly appointed by the Forestry Bureau and the Ministry of Finance. Sino-Forest has not requested such an official valuation of its land, he said. "(The valuation) must have two chops (official seals) and two forestry resource evaluation experts and two licensed evaluators... . Even I can't just go there and give it a value."

[...]

174. The June 19 article, titled "On the trail of the truth behind Sino-Forest," stated in part:

The deepening mystery surrounding Canadian timber company Sino-Forest Corp. leads to the regional capital of Kunming in China's Yunnan province and down Huashan West Road – to an address that doesn't exist.

That address, No. 125 - 129 Huashan West Rd., is listed as the office of a forestry company that sold 1,600 hectares of timber in Yunnan province to a Sino-Forest subsidiary in March. But the odd-numbered side of Huashan West Road ends at 81.

Finding the buyer, the Sino-Forest subsidiary, proves almost as elusive. The office is in a white three-storey building with a green Sino-Panel sign on Bai Tai Road on the northern edge of Lincang, the administrative centre of the region's forestry industry. But it's empty.

The curious transactions totalling \$6-million and inked on March 7 between a Sino-Forest subsidiary with an empty office and a seller with no address highlight the bigger questions surrounding Sino-Forest's dealings in southern China. Trying to penetrate Sino-Forest's complicated business in Yunnan can be like trying to spot the sun through the thick forests of oak, birch, pine and other timber that carpet the mountains in this sprawling region along China's border with Myanmar.

[...]

Senior forestry bureaucrats also told The Globe and Mail that there's no official valuation of Sino-Forest's properties, since the company has never applied to have an evaluation conducted by the local government. The Yunnan Forestry Bureau has since launched an investigation into the company's claims.

[...]

Two weeks of travelling by car and plane to visit Sino-Forest offices, properties and partners in Yunnan, Hunan and Beijing – and interviews with forestry officials, industry experts and local residents – led to as many new questions as answers.

In the series of deals inked on March 7, the buyer was named as Sino-Panel (Yunnan) Forestry Co., the local affiliate of Sino-Forest, and the seller was listed as Yunnan Shunxuan Forestry Co. Ltd. of Huashan West Road.

No one on Huashan West Road recalls a forestry company ever having an office in the area. "If there was a company like this on Huashan West Road, I would know about it," said a member of the neighbourhood committee (a hyperlocal and usually omniscient arm of the ruling Communist Party) that is responsible for the street.

At the same time, neighbours say the office of Sino-Panel on Bai Tai Road sat empty until Thursday, June 2 – hours before Muddy Waters released the report

that rocked investor confidence in Sino-Forest and sent its share price spiralling downwards. Then a moving van arrived at the long-vacant building and began unloading desks, chairs, power bars and Internet cables.

A week later, however, there was still no evidence of anyone working there, other than a squashed cigarette butt and a caulking gun that lay on the dirty tile floor amid the bare workstations.

“We wouldn’t have noticed, but (on June 2) my car was blocking the moving van (and had to be moved). Before that, the building was empty,” said Wu Jie, manager of the regional office of Fanhua Forestry Investments Development Co., which sits beside a massage parlour and an English training centre across the street from the deserted Sino-Panel building.

[...]

175. In the latter article, the *Globe* also discussed Sino’s failure to disclose certain related party transactions.

176. On June 20, 2011, Muddy Waters released a follow-up report, “The Ties that Blind, Part 1: Huaihua Yuda,” which provided further detail on Sino’s undisclosed transactions with related parties Huaihua Yuda and Sonic Jita.

177. When the market closed on June 20, 2011, Sino’s shares traded at \$2.73 (a decline of 85% from June 1, 2011).

178. After the close of markets on June 20, 2011, it was revealed that certain entities affiliated with Paulson & Co., which had been Sino’s largest shareholder, had sold all of its holdings and thereby realized a loss, on a mark-to-market basis, in excess of \$560-million. Only five days earlier, Horsley had sought to reassure investors, saying “I’ve spoken to [Paulson & Co.] and they are very supportive.”

179. The next day, Sino shares closed at \$1.99 a decline of \$16.22 or 89% from their closing price on June 1, 2011.

180. On July 14, 2011, Fitch Ratings withdrew its ratings of Sino’s debt securities, stating:

Fitch Ratings has withdrawn Sino-Forest Corporation's (Sino-Forest) Foreign Currency Issuer Default Rating and senior unsecured debt rating of 'BB-'. The ratings were on Negative Watch at the point of withdrawal. Fitch has withdrawn the ratings as it is unable to obtain sufficient information to maintain them.

[...]

Since placing Sino-Forest on Negative Watch on 20 June 2011, Fitch had requested from the company a more frequent and regular update of its offshore cash balances, as well as updates on management's progress/intentions with regard to the future onshore/offshore structure of the business. Fitch viewed this information as critical to monitoring the position of Sino-Forest offshore creditors, particularly given that under the current business structure offshore obligors are unable to directly access the company's onshore cash flows.

***Management has informed Fitch that the company is unwilling to provide any further information*** until the Committee of Independent Board Members – which was formed to investigate the allegations made by Muddy Waters LLC – publishes its findings. The company has not provided a date for the publication. ***Fitch does not consider these actions commensurate with being able to maintain the rating for investors.***

Fitch will no longer provide ratings or analytical coverage of this issuer.

[Emphasis added.]

181. At the close of trading on August 25, 2011, Sino's shares traded at \$4.81 per share. Shortly prior to the commencement of trading on August 26, 2011, the OSC issued a cease-trade order in relation to Sino's securities, and also took the unprecedented step of ordering, without a hearing, that Chan and various other Sino officers resign.

182. In its order, the OSC stated that in part:

[...]

3. Albert Ip ("Ip") is the Senior Vice President Development and Operations North-East and South-West China of Sino-Forest;
4. Alfred C.T. Hung ("Hung") is Vice-President Corporate Planning and Banking of Sino-Forest;
5. George Ho ("Ho") is Vice-President Finance of Sino-Forest;

6. Simon Yeung (“Yeung”) is Vice President - Operation within the Operation / Project Management group of Sino-Panel (Asia) Inc., a subsidiary of Sino-Forest (“Yeung”);
  7. Since 2003, Sino-Forest has raised approximately \$2.986 billion from public investment and/or debt securities issues including four public offerings between 2004 and 2009 which approximately raised \$1.05 billion;
  8. Sino-Forest has over 150 subsidiaries, the majority of which are registered in the British Virgin Islands and Peoples Republic of China (“PRC”);
  9. Sino-Forest’s operations are predominately in the PRC and its management has offices in Hong Kong primarily and also in the PRC and Ontario;
  10. Staff of the Commission is conducting an investigation into the activities and business of Sino-Forest and its subsidiaries and their management;
  11. The Independent Committee of Sino-Forest has also been conducting an investigation into the activities and business of Sino-Forest and its subsidiaries and their management. As a result, Sino-Forest has recently suspended Ho, Hung, and Yeung temporarily and curtailed Ip’s duties and responsibilities.
  12. Sino-Forest, through its subsidiaries, appears to have engaged in significant non-arm’s length transactions which may have been contrary to Ontario securities laws and the public interest;
  13. Sino-Forest and certain of its officers and directors appear to have misrepresented some of its revenue and/or exaggerated some of its timber holdings by providing information to the public in documents required to be filed or furnished under Ontario securities laws which may have been false or misleading in a material respect contrary to section 122 or 126.2 of the Act and contrary to the public interest;
  14. Sino-Forest and certain of its officers and directors including Chan appear to be engaging or participating in acts, practices or a course of conduct related to its securities which it and/or they know or reasonably ought to know perpetuate a fraud on any person or company contrary to section 126.1 of the Act and contrary to the public interest;
183. Several hours later, the OSC rescinded its order that Chan and the other Sino officers referenced in the preceding paragraph resign, but maintained its cease-trade order.
184. On August 28, 2011, Sino announced that Chan had resigned “voluntarily” from the positions of Sino’s CEO and Board Chairman and as a member of the Sino Board.

### **SINO REWARDS ITS EXPERTS**

185. Sino's Board and management include former E&Y partners and employees, including Bowland, Hyde and West. Boland, Hyde and West serve on the Audit Committee but purported to exercise oversight of their former E&Y colleagues. In addition, Sino's Vice-President, Finance (Corporate), Thomas M. Maradin, is a former E&Y employee.

186. The charter of Sino's Audit Committee required that Ardell, Bowland, Hyde and West "review and take action to eliminate all factors that might impair, or be perceived to impair, the independence of the Auditor." Sino's practice of appointing E&Y personnel to its board – and paying them handsomely (for example, Hyde was paid \$163,623 by Sino in 2010, \$115,962 in 2009, \$57,000 in 2008 and \$55,875 in 2007, plus options and other compensation) – undermined the Audit Committee's oversight of E&Y.

187. E&Y's independence was impaired by the significant non-audit fees it was paid during 2008-2010, which total \$712,000 in 2008, \$1,225,000 in 2009 and \$992,000 in 2010.

188. Further, Andrew Fyfe, the former Asia-Pacific President for Pöyry Forestry Industry Ltd, was appointed Chief Operating Officer of Greenheart, and is the director of several Sino subsidiaries. Fyfe signed various reports produced by Pöyry including those dated June 30, 2004, March 22, 2005, March 23, 2006, March 14, 2008 and April 1, 2009.

189. George Ho, Sino's Vice President, Finance (China), is a former Senior Manager of BDO. BDO was Sino's auditor from March 21, 2005 to August 12, 2007. BDO resigned at Sino's request.

190. Richard Kimel, Sino's Corporate Secretary, is a partner at Aird & Berlis LLP. Kimel replaced Jay Lefton who was at the time also a partner at Aird & Berlis. Aird & Berlis advised Sino in connection with the Offerings.

### **THE PLAINTIFFS' CAUSES OF ACTION**

#### ***Negligent Misrepresentation***

191. As against all Defendants, and on behalf of all Class Members, the Plaintiffs plead negligent misrepresentation.

192. In support of that cause of action, the sole misrepresentation that the Plaintiffs plead is the Representation. The Plaintiffs do not plead any other misrepresentation in support of their negligent misrepresentation claim. For greater clarity, any misrepresentations other than the Representation that are alleged in this Statement of Claim to have been made by some or all of the Defendants during the Class Period are pleaded only in support of the Plaintiffs' claims in negligence simpliciter, unjust enrichment, oppression, conspiracy and pursuant to the Securities Legislation.

193. The Representation is contained in the phrase "[e]xcept where otherwise indicated, all financial information reflected herein is determined on the basis of Canadian generally accepted accounting principles ("GAAP")." This phrase appears in the every annual and quarterly MD&A that is an Impugned Document. Sino and the Individual Defendants made this statement or caused it to be made.

194. The Representation is also contained in the phrase "[t]he consolidated financial statements of Sino-Forest Corporation (the "Company") have been prepared [...] in accordance with Canadian generally accepted accounting principles." This phrase appears in every Audited



Annual Financial Statement that is an Impugned Document. Every Interim Financial Statement that is an Impugned Document incorporated by reference that section of the relevant Audited Annual Financial Statement which contained that phrase. Sino and the Individual Defendants made this statement, approved it and/or caused it to be made.

195. The Representation is also contained in the phrase “[t]he consolidated financial statements contained in this Annual Report have been prepared by management in accordance with Canadian generally accepted accounting principles.” This phrase appears in every Audited Annual Financial Statement that is an Impugned Document. That statement was made by Sino, Chan and Horsley in the “Management’s Report.” The other Individual Defendants approved the statement and/or caused it to be made.

196. The Representation is contained in the phrase “[w]e prepare our financial statements in accordance with Canadian GAAP” found in the AIFs filed on March 31, 2009 and 2010. The Representation is also contained in the phrase “[p]rior to January 1, 2011, we have prepared our financial statements in accordance with Canadian GAAP” found in the AIF filed on March 31, 2011. The Impugned Documents that are Management Information Circulars incorporated the most recent AIF, Annual MD&A and Annual Financial Statements by reference and thus the Representation. Sino and the Individual Defendants made these statements, approved them and/or caused them to be made.

197. The Representation is further contained in the phrase “[t]he Corporation prepares its financial statements in accordance with Canadian GAAP” found in the Prospectuses. Sino and the Individual Defendants made this statement, approved it and/or caused it to be made.

198. The Representation is contained in the phrase “[i]n our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company

as at December 31, [years vary between documents] and the results of its operations and its cash flows for the year[s] then ended in accordance with Canadian generally accepted accounting principles,” made by E&Y in every Audited Annual Financial Statement that is an Impugned Document.

199. The Representation was untrue: the Impugned Documents violated GAAP by, among other things, overstating to a material degree Sino’s revenues, net income and assets, failing to disclose changes in accounting policies, understating Sino’s tax accruals, and failing to disclose related party transactions.

200. The Impugned Documents were prepared for the purpose of attracting investment and inducing members of the investing public to purchase Sino securities, and all of the Defendants knew at all material times that those documents had been prepared for that purpose, and that the Class Members would rely reasonably and to their detriment upon such documents in making the decision to purchase Sino securities.

201. The Defendants further knew that the information contained in the Impugned Documents would be incorporated into the price of Sino’s publicly traded securities such that the trading price of those securities would at all times reflect the information contained in the Impugned Documents.

202. By virtue of their purported accounting, financial and/or managerial acumen and qualifications, and by virtue of their having assumed, voluntarily and for profit, the role of gatekeepers, the Defendants had a duty at common law, informed by the Securities Legislation, to exercise care and diligence to ensure that the Impugned Documents fairly and accurately disclosed Sino’s financial condition and performance in accordance with GAAP.

203. The Defendants or some of them breached that duty by making the Representation as particularized above.

204. The Plaintiffs and the other Class Members directly or indirectly relied upon the Representation in making a decision to purchase the securities of Sino.

205. Alternatively, the Plaintiffs and the other Class Members relied upon the Representation by the act of purchasing Sino securities in an efficient market that promptly incorporated into the price of those securities all publicly available material information regarding the securities of Sino. As a result, Sino's repeated publication of the Representation in the Impugned Documents caused the price of Sino's shares to trade at inflated prices during the Class Period, thus directly resulting in damage to the Plaintiffs and Class Members.

***Statutory Claims, Negligence, Oppression, Unjust Enrichment and Conspiracy***

***Statutory Liability– Secondary Market***

206. The Plaintiffs intend to deliver a notice of motion seeking, among other things, an order granting leave to bring the statutory causes of action found in Part XXIII.1 of the *OSA*, and, if required, the equivalent sections of the Securities Legislation other than the *OSA*, against all Defendants except the Underwriters.

207. Each of the Impugned Documents is a “Core Document” within the meaning of the Securities Legislation.

208. Each of the Impugned Documents contained one or more misrepresentations as particularized above. The Representation is a misrepresentation for the purposes of the Securities Legislation.

209. Each of the Individual Defendants was an officer and/or director of Sino at material times. Each of the Individual Defendants authorized, permitted or acquiesced in the release of some or all of the Impugned Documents.

210. Sino is a reporting issuer within the meaning of the Securities Legislation.

211. E&Y is an expert within the meaning of the Securities Legislation. E&Y consented to the use of its statements particularized above in the Impugned Documents.

212. Pöyry is an expert within the meaning of the Securities Legislation. Pöyry consented to the use of its statements particularized above in the Impugned Documents.

213. At all times material to the matters complained of herein, each of Sino, Chan, Poon, Horsley and E&Y knew or, at a minimum, were wilfully blind to the fact that the Impugned Documents contained the Representation and that the Representation was false, and that the Impugned Documents contained other of the misrepresentations that are alleged above to have been contained therein.

***Statutory Liability – Primary Market***

214. As against the Defendants who signed the June 2009 and/or December 2009 Prospectuses or who consented to the inclusion therein of their opinions and reports, and on behalf of those Class Members who purchased Sino shares in one of the distributions to which those Prospectuses related, Labourers asserts the cause of action set forth in s. 130 of the *OSA* and, if necessary, the equivalent provisions of the Securities Legislation other than the *OSA*.

215. Sino issued the June 2009 and December 2009 Prospectuses, which contained the Representation and the other misrepresentations that are alleged above to have been contained in those Prospectuses or in the Sino disclosure documents incorporated therein by reference.

*Negligence Simpliciter – Primary Market*

216. As against the Defendants who signed one or more of the Prospectuses or who consented to the inclusion therein of their opinions and reports, and on behalf of those Class Members who purchased Sino shares in one of the distributions to which those Prospectuses related, Labourers asserts negligence simpliciter.

217. Sino, E&Y, Poyry, the Underwriters and, by virtue of their position of authority and responsibility within Sino, each of the Individual Defendants, owed a duty to the Plaintiffs and to persons and entities similarly situated, at law and under provisions of the *OSA* and the Securities Legislation, to ensure that the Prospectuses they signed made full, true and plain disclosure of all material facts relating to the securities offered thereby, or to ensure that their opinions or reports contained in such Prospectuses did not contain a misrepresentation.

218. At all times material to the matters complained of herein, the Defendants who signed one or more of the Prospectuses, or who consented to the use therein of their report or opinion, ought to have known that such Prospectuses and the documents incorporated therein by reference were materially misleading in that they contained the Representation and the other misrepresentations particularized above.

219. Accordingly, the Defendants have violated their duties to those Class Members who purchased Sino shares in a distribution to which a Prospectus related.

220. The reasonable standard of care expected in the circumstances required the Defendants to prevent the distributions to which the Prospectuses related from occurring prior to the correction of the Representation and the other misrepresentations alleged above to have been contained in the Prospectuses or in the documents incorporated therein by reference. The Defendants failed

to meet the standard of care required by causing the Offerings to occur before the correction of such misrepresentations.

221. In addition, by failing to attend and participate in Sino board and board committee meetings to a reasonable degree, Murray and Poon effectively abdicated their duties to the Class Members and as directors of Sino.

222. Further, Sino, E&Y and the Individual Defendants further breached their duty of care as they failed to maintain appropriate internal controls to ensure that Sino's disclosure documents adequately and fairly presented the business and affairs of Sino on a timely basis.

223. Had the Defendants exercised reasonable care and diligence in connection with the distributions to which the Prospectuses related, then securities regulators likely would not have issued a receipt for any of the Prospectuses, and those distributions would not have occurred, or would have occurred at prices that reflected the true value of Sino's shares.

224. The Defendants' negligence in relation to the Prospectuses resulted in damage to Labourers and to the other Class Members who purchased Sino shares in the related distributions. Had the Defendants' satisfied their duty of care to such Class Members, then those Class Members would not have purchased the shares that they acquired under the Prospectuses, or they would have purchased them at a much lower price that reflected their true value.

***Unjust Enrichment of Chan, Martin, Poon, Horsley, Mak and Murray***

225. As a result of the Representation and the other misrepresentations particularized above, Sino's shares traded, and were sold by Chan, Martin, Poon, Horsley, Mak and Murray, at artificially inflated prices during the Class Period.

226. Accordingly, Chan, Martin, Poon, Horsley, Mak and Murray were enriched by their wrongful acts and omissions during the Class Period, and the Class Members who purchased Sino shares from such Defendants suffered a corresponding deprivation.

227. There was no juristic reason for the resulting enrichment of Chan, Martin, Poon, Horsley, Mak and Murray.

228. Accordingly, the Class Members who purchased Sino shares from Chan, Martin, Poon, Horsley, Mak and Murray during the Class Period are entitled to the difference between the price they paid to such Defendants for such shares, and the price that they would have paid had the Defendants not made the Representation and the other misrepresentations particularized above, and had not committed the wrongful acts and omissions particularized above.

***Unjust Enrichment of Sino***

229. Throughout the Class Period, Sino made the Offerings. Such Offerings were made via various documents, particularized above, that contained the Representation and the misrepresentations particularized above.

230. The securities sold by Sino via the Offerings were sold at artificially inflated prices as a result of the Representation and the others misrepresentations particularized above.

231. Sino was enriched by, and those Class Members who purchased securities via the Offerings were deprived of, an amount equivalent to the difference between the amount for which the securities offered were actually sold, and the amount for which such securities would have been sold had the Offerings not included the Representation and the misrepresentations particularized above.

232. The Offerings violated Sino's disclosure obligations under the Securities Legislation and the various instruments promulgated by the securities regulators of the Provinces in which such Offerings were made. There was no juristic reason for the enrichment of Sino.

***Unjust Enrichment of the Underwriters***

233. Throughout the Class Period, Sino made the Offerings. Such Offerings were made via various documents, particularized above, that contained the Representation and the other misrepresentations particularized above. The Underwriters underwrote certain of the Offerings, including those conducted pursuant to the Prospectuses.

234. The securities sold by Sino via the Offerings were sold at artificially inflated prices as a result of the Representation and the other misrepresentations particularized above. The Underwriters earned fees from the Class, whether directly or indirectly, for work that they never performed or that they performed with gross negligence, in connection with the Offerings, or some of them.

235. The Underwriters was enriched by, and those Class Members who purchased securities via the Offerings were deprived of, an amount equivalent to the fees the Underwriters earned in connection with the Offerings.

236. The Offerings violated Sino's disclosure obligations under the Securities Legislation and the various instruments promulgated by the securities regulators of the Provinces in which such Offerings were made. There was no juristic reason for the enrichment of the Underwriters.

237. In addition, some or all of the Underwriters also acted as brokers in secondary market transactions relating to Sino securities, and earned trading commissions from the Class Members in those secondary market transactions in Sino securities. Those Underwriters were enriched by, and those Class Members who purchased Sino securities through those Underwriters in their



capacity as brokers were deprived of, an amount equivalent to the commissions the Underwriters earned on such secondary market trades.

238. Had those Underwriters who also acted as brokers in secondary market transactions exercised reasonable diligence in connection with the Offerings in which they acted as Underwriters, then Sino's securities likely would not have traded at all in the secondary market, and the Underwriters would not have been paid the aforesaid trading commissions by the Class Members. There was no juristic reason for that enrichment of those Underwriters through their receipt of trading commissions from the Class Members.

***Oppression***

239. In the circumstances alleged herein, the Plaintiffs and the other Class Members had a reasonable and legitimate expectation that Sino and the Individual Defendants would use their powers to direct the company for Sino's best interests and, in turn, in the interests of its security holders. More specifically, the Plaintiffs and the other Class Members had a reasonable expectation that:

- (a) Sino and the Individual Defendants would comply with GAAP, and/or cause Sino to comply with GAAP;
- (b) Sino and the Individual Defendants would take reasonable steps to ensure that the Class Members were made aware on a timely basis of material developments in Sino's business and affairs;
- (c) Sino and the Individual Defendants would implement adequate corporate governance procedures and internal controls to ensure that Sino disclosed material facts and material changes in the company's business and affairs on a timely basis;

- (d) Sino and the Individual Defendants would not make the misrepresentations particularized above;
- (e) Sino stock options would not be backdated or otherwise mispriced; and
- (f) the Individual Defendants would adhere to the Code.

240. Such reasonable expectations were not met as:

- (a) Sino did not comply with GAAP;
- (b) the Class Members were not made aware on a timely basis of material developments in Sino's business and affairs;
- (c) Sino's corporate governance procedures and internal controls were inadequate;
- (d) the misrepresentations particularized above were made;
- (e) stock options were backdated and/or otherwise mispriced; and
- (f) the Individual Defendants did not adhere to the Code

241. Sino's and the Individual Defendants' conduct was oppressive and unfairly prejudicial to the Plaintiffs and the other Class Members and unfairly disregarded their interests. These defendants were charged with the operation of Sino for the benefit of all of its shareholders.

The value of the shareholders' investments was based on, among other things:

- (a) the profitability of Sino;
- (b) the integrity of Sino's management and its ability to run the company in the interests of all shareholders;
- (c) Sino's compliance with its disclosure obligations;

- (d) Sino's ongoing representation that its corporate governance procedures met with reasonable standards, and that the business of the company was subjected to reasonable scrutiny; and
- (e) Sino's ongoing representation that its affairs and financial reporting were being conducted in accordance with GAAP.

242. This oppressive conduct impaired the ability of the Plaintiffs and other Class Members to make informed investment decisions about Sino's securities. But for that conduct, the Plaintiffs and the other Class Members would not have suffered the damages alleged herein.

***Conspiracy***

243. Sino, Chan, Poon and Horsley conspired with each other and with persons unknown (collectively, the "**Conspirators**") to inflate the price of Sino's securities. During the Class Period, the Conspirators unlawfully, maliciously and lacking bona fides, agreed together to, among other things, make the Representation and other misrepresentations particularized above.

244. Some, but not all, of the Conspirators' predominant purposes, concerns and motivations in so conspiring were to:

- (a) inflate the price of Sino's securities, or alternatively, maintain an artificially high trading price for Sino's securities;
- (b) artificially increase the value of the securities they held; and
- (c) inflate that portion of their compensation was dependent in whole or in part upon the performance of Sino and its securities.

245. In furtherance of the conspiracy, the following are some, but not all, of the acts carried out or caused to be carried out by the Conspirators, or some of them:

- (a) they agreed to, and did, make the Representation, which they knew was false;

- (b) they agreed to, and did, make the other misrepresentations particularized above, which they knew were false;
- (c) they caused Sino to issue the Impugned Documents which they knew to be materially misleading;
- (d) as alleged more particularly below, they caused to be issued stock options in respect of which the strike price was impermissibly low; and
- (e) they authorized the sale of securities pursuant to Prospectuses and Offering Memoranda that they knew to be materially false and misleading.

246. Stock options are a form of compensation used by companies to incentivize the performance of directors, officers and employees. Options are granted on a certain date (the 'grant date') at a certain price (the 'exercise' or 'strike' price). At some point in the future, typically following a vesting period, an options-holder may, by paying the strike price, exercise the option and convert the option into a share in the company. The option-holder will make money as long as the option's strike price is lower than the market price of the security at the moment that the option is exercised. This enhances the incentive of the option recipient to work to raise the stock price of the company.

247. There are three types of option grants:

- (a) 'in-the-money' grants are options granted where the strike price is lower than the market price of the security on the date of the grant; such options are not permissible under the TSX Rules and have been prohibited by the TSX Rules at all material times;
- (b) 'at-the-money' grants are options granted where the strike price is equal to the market price of the security on the date of the grant or the closing price the day prior to the grant; and

- (c) 'out-of-the-money' grants are options granted where the strike price is higher than the market price of the security on the date of the grant.

248. Both at-the-money and out-of-the-money options are permissible under the TSX Rules and have been at all material times.

249. The purpose of both at-the-money and out-of-the-money options is to create incentives for option recipients to work to raise the share price of the company. Such options have limited value at the time of the grant, because they entitle the recipient to acquire the company's shares at or above the price at which the recipient could acquire the company's shares in the open market. Options that are in-the-money, however, have substantial value at the time of the grant irrespective of whether the company's stock price rises subsequent to the grant date.

250. At all material times, the Sino Option Plan (the "**Plan**") prohibited in-the-money options.

251. The Conspirators backdated and/or otherwise mispriced Sino stock options, or caused the backdating and/or mispricing of Sino stock options, in violation of, inter alia: (a) the *OSA* and the rules and regulations promulgated thereunder; (b) the Plan; (c) GAAP; (d) the Code; (e) the TSX Rules; and (f) the Conspirators' statutory, common law and contractual fiduciary duties and duties of care to Sino and its shareholders, including the Class Members.

252. The Sino stock options that were backdated or otherwise mispriced included those issued on June 26, 1996 to Chan, January 21, 2005 to Horsley, September 14, 2005 to Horsley, June 4, 2007 to Horsley and Chan, August 21, 2007 to Sino insiders other than the Conspirators, November 23, 2007 to George Ho and other Sino insiders, and March 31, 2009 to Sino insiders other than the Conspirators.

253. The graph below shows the average stock price returns for fifteen trading days prior and subsequent to the dates as of which Sino priced its stock options to its insiders. As appears

therefrom, on average the dates as of which Sino's stock options were priced were preceded by a substantial decline in Sino's stock price, and were followed by a dramatic increase in Sino's stock price. This pattern could not plausibly be the result of chance.



254. The conspiracy was unlawful because the Conspirators knowingly and intentionally committed the foregoing acts when they knew such conduct was in violation of, *inter alia*, the *OSA*, the Securities Legislation other than the *OSA*, the Code, the rules and requirements of the TSX (the “**TSX Rules**”) and the *CBCA*. The Conspirators intended to, and did, harm the Class by causing artificial inflation in the price of Sino's securities.

255. The Conspirators directed the conspiracy toward the Plaintiffs and the other Class Members. The Conspirators knew in the circumstances that the conspiracy would, and did, cause loss to the Plaintiffs and the other Class Members.

**THE RELATIONSHIP BETWEEN SINO'S DISCLOSURES AND THE PRICE OF SINO'S SECURITIES**

256. The price of Sino's securities was directly affected during the Class Period by the issuance of the Impugned Documents. The Defendants were aware at all material times of the effect of Sino's disclosure documents upon the price of its Sino's securities.

257. The Impugned Documents were filed, among other places, with SEDAR and the TSX, and thereby became immediately available to, and were reproduced for inspection by, the Class Members, other members of the investing public, financial analysts and the financial press.

258. Sino routinely transmitted the documents referred to above to the financial press, financial analysts and certain prospective and actual holders of Sino securities. Sino provided either copies of the above referenced documents or links thereto on its website.

259. Sino regularly communicated with the public investors and financial analysts via established market communication mechanisms, including through regular disseminations of their disclosure documents, including press releases on newswire services in Canada, the United States and elsewhere. Each time Sino communicated that new material information about Sino financial results to the public the price of Sino securities was directly affected.

260. Sino was the subject of analysts' reports that incorporated certain of the material information contained in the Impugned Documents, with the effect that any recommendations to purchase Sino securities in such reports during the Class Period were based, in whole or in part, upon that information.

261. Sino's securities were and are traded, among other places, on the TSX, which is a efficient and automated market. The price at which Sino's securities traded promptly incorporated material information from Sino's disclosure documents about Sino's business and

affairs, including the Representation, which was disseminated to the public through the documents referred to above and distributed by Sino, as well as by other means.

### **VICARIOUS LIABILITY**

#### ***Sino and the Individual Defendants***

262. Sino is vicariously liable for the acts and omissions of the Individual Defendants particularized in this Claim.

263. The acts or omissions particularized and alleged in this Claim to have been done by Sino were authorized, ordered and done by the Individual Defendants and other agents, employees and representatives of Sino, while engaged in the management, direction, control and transaction of the business and affairs of Sino. Such acts and omissions are, therefore, not only the acts and omissions of the Individual Defendants, but are also the acts and omissions of Sino.

264. At all material times, the Individual Defendants were officers and/or directors of Sino. As their acts and omissions are independently tortious, they are personally liable for same to the Plaintiffs and the other Class Members.

#### ***E&Y***

265. E&Y is vicariously liable for the acts and omissions of each of its officers, directors, partners, agents and employees as set out above.

266. The acts or omissions particularized and alleged in this Claim to have been done by E&Y were authorized, ordered and done by its officers, directors, partners, agents and employees, while engaged in the management, direction, control and transaction of the business and affairs of E&Y. Such acts and omissions are, therefore, not only the acts and omissions of those persons, but are also the acts and omissions of E&Y.



***Pöyry***

267. Pöyry is vicariously liable for the acts and omissions of each of its officers, directors, partners, agents and employees as set out above.

268. The acts or omissions particularized and alleged in this Claim to have been done by Pöyry were authorized, ordered and done by its officers, directors, partners, agents and employees, while engaged in the management, direction, control and transaction of the business and affairs of Pöyry. Such acts and omissions are, therefore, not only the acts and omissions of those persons, but are also the acts and omissions of Pöyry.

***The Underwriters***

269. The Underwriters are vicariously liable for the acts and omissions of each of their respective officers, directors, partners, agents and employees as set out above.

270. The acts or omissions particularized and alleged in this Claim to have been done by the Underwriters were authorized, ordered and done by each of their respective officers, directors, partners, agents and employees, while engaged in the management, direction, control and transaction of the business and affairs such Underwriters. Such acts and omissions are, therefore, not only the acts and omissions of those persons, but are also the acts and omissions of the respective Underwriters.

**REAL AND SUBSTANTIAL CONNECTION WITH ONTARIO**

271. The Plaintiffs plead that this action has a real and substantial connection with Ontario because, among other thing:

- (a) Sino is a reporting issuer in Ontario;
- (b) Sino's shares trade on the TSX which is located in Toronto, Ontario;
- (c) Sino's registered office and principal business office is in Mississauga, Ontario;

- (d) the Sino disclosure documents referred to herein were disseminated in and from Ontario;
- (e) a substantial proportion of the Class Members reside in Ontario;
- (f) Sino carries on business in Ontario; and
- (g) a substantial portion of the damages sustained by the Class were sustained by persons and entities domiciled in Ontario.

### **SERVICE OUTSIDE OF ONTARIO**

272. The Plaintiffs may serve the Notice of Action and Statement of Claim outside of Ontario without leave in accordance with rule 17.02 of the Rules of Civil Procedure, because this claim is:

- (a) a claim in respect of personal property in Ontario (para 17.02(a));
- (b) a claim in respect of damage sustained in Ontario (para 17.02(h));
- (c) a claim authorized by statute to be made against a person outside of Ontario by a proceeding in Ontario (para 17.02(n)); and
- (d) a claim against a person outside of Ontario who is a necessary or proper party to a proceeding properly brought against another person served in Ontario (para 17.02(o)); and
- (e) a claim against a person ordinarily resident or carrying on business in Ontario (para 17.02(p)).

**RELEVANT LEGISLATION, PLACE OF TRIAL & JURY TRIAL**

273. The Plaintiffs plead and rely on the *CJA*, the *CPA*, the Securities Legislation and *CBCA*, all as amended.

274. The Plaintiffs propose that this action be tried in the City of Toronto, in the Province of Ontario, as a proceeding under the *CPA*.

275. The Plaintiffs will serve a jury notice.

August 30, 2011

**Siskinds LLP**

Barristers & Solicitors  
680 Waterloo Street  
P.O. Box 2520  
London, ON N6A 3V8

A. Dimitri Lascaris (LSUC#: 50074A)

Tel: 519.660.7844

Fax: 519.660.7845

Michael G. Robb (LSUC#: 45787G)

Tel: 519.660.7872

Fax: 519.660.7873

Daniel E. H. Bach (LSUC #: 52087E)

Tel: 416.362.8334

Fax: 416.362.2610

**Koskie Minsky LLP**

20 Queen Street West, Suite 900, Box 52  
Toronto, ON M5H 3R3

Kirk M. Baert (LSUC#: 30942O)

Tel: 416.595.2117

Fax: 416.204.2889

Jonathan Ptak (LSUC#: 45773F)

Tel: 416-595.2149

Fax: 416.204.2903

Lawyers for the Plaintiffs

Trustees of the Labourers' Pension Fund of Central and Eastern Canada  
and The Board of Trustees of the International Union of Operating  
Engineers, Local 793, Members Life and Health Benefit Trust Fund  
Plaintiffs

and

Sino-Forest Corporation,  
*et al.*

Defendants

Court File No.: CV-11-431153-00CP

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

Proceeding commenced at Toronto  
Proceeding under the *Class Proceedings Act, 1992*

**STATEMENT OF CLAIM  
(NOTICE OF ACTION ISSUED JULY 20, 2011)**

**Siskinds LLP**

Barristers & Solicitors  
680 Waterloo Street  
P.O. Box 2520  
London, ON N6A 3V8

A. Dimitri Lascaris (LSUC#: 50074A)  
Tel: 519.660.7844  
Fax: 519.660.7845  
Michael G. Robb (LSUC#: 45787G)  
Tel: 519.660.7872  
Fax: 519.660.7873  
Daniel E.H. Bach (LSUC #: 52087E)  
Tel: 416.362.8334  
Fax: 416.362.2610

**Koskie Minsky LLP**

20 Queen Street West, Suite 900, Box 52  
Toronto, ON M5H 3R3

Kirk M. Baert (LSUC#: 30942O)  
Tel: 416.595.2117  
Fax: 416.204.2889  
Jonathan Ptak (LSUC#: 45773F)  
Tel: 416-595.2149  
Fax: 416.204.2903  
Lawyers for the Plaintiffs