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NQ Admits Widespread Data Tampering, but Claims it is not a Fraud

(Committee to NQ: During the course of our fraud investigation, we caught you trying to defraud us.)

NQ admitted widespread tampering with data reviewed during the investigation. The press release reads:

“Despite the Investigation Team’s extensive review of documents and data provided by sources both within and outside the Company, the Investigation Team could not verify that the devices it collected and copied contained all responsive information at the time the copies were made. On many devices, the Investigation Team observed indications that some information might be missing, and the Company’s management and staff were unable to provide a credible explanation for what the Investigation Team observed.”

This disclosure is reminiscent of the final report delivered by Sino-Forest’s “independent” committee. The Sino-Forest directors’ conclusion was that they could find no evidence to support Muddy Waters’s fraud allegations.¹ Sino-Forest’s exculpatory press release read:

“The Independent Committee report verifies the Company’s stated cash balances, confirms registered title or contractual rights to the Company’s stated timber assets, as well as the book value of these assets, reconciles reported total revenue and refutes the allegation that Yuda Wood is a subsidiary of the Company. We can categorically say Sino-Forest is not the ‘near total fraud’ and ‘Ponzi scheme’ as alleged by Muddy Waters.”

With a couple of name substitutions, the above statement would mirror that put out by NQ. Unlike NQ, Sino-Forest did release a redacted version of the directors’ report. That report alluded to the evidence tampering that Sino-Forest management undertook, which appears similar to that undertaken by NQ.² It cited problems, including:

- “data on some servers in China appearing to have been deleted on an irregular basis, and there is no back-up system;”
- “lack of full cooperation/openness in the ICs examination from certain members of Management.”

¹ <http://www.prnewswire.com/news-releases/sino-forest-announces-findings-of-the-independent-committee-133859828.html>

² See November 13, 2011 “Interim Report of the Independent Committee of Directors of the Sino-Forest Corporation”

The Sino-Forest committee's conclusion that it could find no evidence of fraud has now been thoroughly discredited. The Ontario Securities Commission is suing the former management for fraud. Just two weeks ago, Sino-Forest's creditors filed suit against its former chairman Allen Chan for \$3 billion. In the complaint (available to download at http://www.muddywatersresearch.com/wp-content/uploads/2014/06/SFC_Litigation_Trust_v_Chen_Claim.pdf), the plaintiff dismisses the independent directors' conclusion, and cites the data tampering as evidence of fraud. It is a sad commentary on how insulated corporate directors are from responsibility that they can publicly conclude there is no evidence of fraud after conducting an investigation in which management was caught defrauding the investigators.

This press release took seven and a half months to come out. Given that there was data tampering during an investigation that dragged on far longer than should have been allowed, it is clear that management was able to stay a step ahead of the investigation by changing and deleting data.

Muddy Waters offered to pay for well-regarded investigative accounting firm Plante & Moran PLLC to write an evaluation report of the investigation, which we would publish. The committee declined the offer.

There are far more questions posed than answered by NQ's press release. The admission of data tampering was undoubtedly the result of a negotiation between the advisors and the company, and which despite making it clear that the tampering was widespread, almost certainly understates the severity of the problem. Unless NQ chooses to provide the level of transparency that Sino-Forest did and release the actual report, we are unlikely to ever learn details about the tampering because the work is shrouded by attorney-client privilege.