STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has publicly reprimanded China Rise Securities Asset Management Company Limited (**China Rise**), formerly known as China Rise Securities Company Limited, and fined it $6.3 million pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).

2. The disciplinary action relates to China Rise's internal control deficiencies and regulatory breaches in relation to short selling, cross trades and keeping of records during the period from January to May 2014 (**1st Relevant Period**) and from January 2015 to August 2016 (**2nd Relevant Period**). Specifically, China Rise failed to:

   (a) put in place adequate system and control procedures to detect and prevent illegal short selling by its staff;

   (b) implement effective internal controls to monitor cross trades between its staff members and clients that gave rise to conflicts of interest, and ensure fair treatment of clients;

   (c) report cross trades to The Stock Exchange of Hong Kong Limited (**Exchange**) in compliance with the Rules of the Exchange; and

   (d) maintain proper records of order placing instructions and its compliance checks.

Summary of facts and breaches

A. Inadequate system and control procedures to detect and prevent short selling

3. China Rise had two trading systems, namely the Multi-workstation System (**MWS**) and the Broker Supplied System (**BSS**). Whilst the BSS possessed the functions to prevent the placing of short selling orders, the MWS did not.

4. During the 1st Relevant Period, China Rise's then chief executive officer and responsible officer (**RO**), Mr. Sammy Shiu Kin Keung (**Shiu**), placed a total of 199 illegal short selling orders involving 21 listed securities for his personal account and a client's discretionary account via the MWS, resulting in 200 short sales executed by China Rise.

5. On 8 June 2017, Shiu was convicted of 14 charges of illegal short selling in breach of section 170 of the SFO, which prohibits a person from selling securities unless at the time of sale, he has a presently exercisable and unconditional right to vest the securities in the purchaser, or believes and has reasonable grounds to believe that he has such a right.

6. Although China Rise's internal policy required its staff members to obtain special approval before executing any short sale, it did not spell out the procedures for obtaining and the criteria for granting such approval. The policy was never

enforced by China Rise and completely disregarded by its staff members, including Shiu.

7. Further, while China Rise purportedly required its staff members to obtain prior approval by way of an application form before placing any orders for their own accounts, in reality:

   (a) there was no such application form and the staff merely used the dealing tickets, which contained very limited information, to obtain approval;

   (b) the RO responsible for monitoring Shiu's personal dealing would approve any dealing tickets submitted by Shiu without checking whether there were any irregularities; and

   (c) Shiu had traded for his own account without seeking another RO's prior approval and such non-compliance was not detected by the RO who was also responsible for reviewing trading activities in staff accounts.

8. China Rise was unaware of the frequent and large number of short selling orders placed by Shiu until Hong Kong Exchange and Clearing Limited (**HKEx**) and the SFC made enquiries about the relevant transactions. Even after HKEx's initial enquiry in early April 2014, nothing was done by China Rise to strengthen its internal controls to prevent further breaches. As a result, Shiu was able to continue his short selling activities without being detected by China Rise.

9. In short, China Rise did not have adequate system and control procedures to detect and prevent short selling, which was in breach of:

   (a) paragraphs 1 and 4 of Part I and paragraph 8 of Part VII of the Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC (**Internal Control Guidelines**), which require the management of a licensed corporation to:

      (i) assume full responsibility for the firm's operations including the development, implementation and on-going effectiveness of the firm's internal controls and the adherence thereto by its directors and employees;

      (ii) ensure that detailed policies and procedures pertaining to authorizations and approvals are clearly defined and communicated to and followed by the staff; and

      (iii) establish and maintain appropriate and effective procedures in relation to dealing and related review processes to prevent or detect errors, omissions, fraud and other unauthorized or improper activities;

   (b) General Principle (**GP**) 3 and paragraph 4.3 of the Code of Conduct for Persons Licensed by or Registered with the SFC (**Code of Conduct**), which provide that a licensed corporation should:

      (i) have and employ effectively the resources and procedures which are needed for the proper performance of its business activities; and

(ii) have internal control procedures and operational capabilities which can reasonably be expected to protect its operations, its clients and other licensed persons from financial loss arising from theft, fraud, and other dishonest acts, professional misconduct or omissions; and

(c) GP 9 and paragraph 12.2(b)(vi) of the Code of Conduct, which provide that senior management of a licensed corporation should:

(i) bear primary responsibility for ensuring maintenance of appropriate standards of conduct and adherence to proper procedures by the firm; and

(ii) actively monitor transactions of employees' account and maintain procedures to detect irregularities and ensure that the handling of these transactions or orders is not prejudicial to the interests of other clients.

B. Lack of internal controls to monitor cross trades between staff members and clients and ensure fair treatment of clients

10. A former member of the senior management of China Rise (**X**) was authorized by a client to conduct discretionary trading in the client's account, and he executed nine pairs of cross trades in eight listed securities between his personal account and the client's account during the 1st Relevant Period (**Nine Cross Trades**).

11. Among the Nine Cross Trades, eight of the transactions were executed at a price favourable to X and detrimental to the client when compared to the nominal price at the time of the transactions.

12. Whilst it was China Rise's policy that cross trades between staff members and clients would only be permitted if prior approval from an RO was obtained, X was able to conduct cross trades with his client without an RO's approval. Even when X submitted dealing tickets to the RO for approval, that RO did not check whether the transactions constituted cross trades or take any steps to ensure that the client was fairly treated.

13. China Rise's monitoring of employee dealings was ineffective. It purportedly prohibited any staff member from dealing in any securities if doing so would give rise to actual or potential conflict of interest. Nonetheless, it failed to detect or prevent the Nine Cross Trades, which were executed by X without disclosing his interest to or obtaining consent from the client.

14. Furthermore, there was a lack of supervision over the operation of discretionary accounts. China Rise's compliance officer neither performed any compliance checks nor reviewed the transactions conducted in discretionary accounts. The RO responsible for monitoring discretionary accounts also failed to detect the Nine Cross Trades.

15. In short, China Rise failed to maintain any controls which could effectively avoid or minimize the conflicts of interest involved in cross trades between an account executive (**AE**) and a client whose discretionary account was operated by that AE, which was in breach of:

(a) paragraphs 4 and 5 of Part VII of the Internal Control Guidelines, which require management to establish and maintain specific policies and procedures to ensure that:

    (i) potential conflict of interest between the firm or its staff and clients is minimized;

    (ii) in circumstances where actual or apparent conflicts of interest cannot reasonably be avoided, clients are fully informed of the nature and possible ramifications of such conflicts and are in all cases treated fairly; and

    (iii) whenever the firm or its staff members have a material interest in a transaction with a client, this fact is disclosed to the client prior to the execution of the relevant transaction;

(b) GP 6 of the Code of Conduct, which provides that a licensed corporation should try to avoid conflicts of interests, and when they cannot be avoided, should ensure that its clients are fairly treated;

(c) paragraph 7.1(e) of the Code of Conduct, which requires a licensed corporation to implement internal control procedures to ensure proper supervision of the operation of discretionary accounts; and

(d) paragraph 1 of Part I of the Internal Control Guidelines, and GP 3, GP 9, and paragraphs 4.3 and 12.2(b)(vi) of the Code of Conduct (see paragraph 9 above).

C. Failure to report cross trades to the Exchange

16. In accordance with Rule 526(1) of the Rules of the Exchange, China Rise's policy required its staff members to report cross trades to the Exchange through inputting the transactions into the trading system within 15 minutes after the conclusion of the same.

17. Nonetheless, China Rise did not have any controls to ensure that its staff members adhered to this policy. X failed to comply with the policy and Rule 526(1) four times during the 1st Relevant Period. None of these breaches was detected by China Rise.

18. China Rise's failure to report cross trades in compliance with the Rules of the Exchange was in breach of GP 7 and paragraph 12.1 of the Code of Conduct, which requires a licensed corporation to comply with, and implement and maintain measures appropriate to ensuring compliance with all regulatory requirements applicable to the conduct of its business activities, including the rules of any exchange of which it is a participant.

D. Lack of records of order placing instructions and compliance checks

19. China Rise claimed that all orders placed through the MWS were supported by filling in and time-stamping of dealing tickets. However, it failed to locate the dealing tickets in relation to at least 100 orders placed by X for his personal account and his client's account during the 1st Relevant Period via the MWS

allegedly due to office relocation and resignation of several back office staff members.

20. The SFC's investigation also revealed that China Rise did not keep order placing instructions records for over 1,000 client orders between February and August 2016. Specifically, China Rise was unable to identify how 762 client orders were placed as no records of clients' instructions (such as dealing tickets or dealing sheets) could be located. In relation to 248 of its client orders, China Rise could not provide tape recordings to evidence the telephone instructions purportedly received from its clients.

21. A large number of missing tape recordings related to orders from one client who called the mobile or non-office phone numbers of her AE. This suggests that China Rise failed to ensure either that a recorded line would be used or when orders were received by mobile phones, its staff would call back to the office's tape recording system.

22. Notwithstanding the large scale of missing records to evidence instructions from clients, China Rise failed to identify any breaches of order recording in the course of its regular compliance check during the 2nd Relevant Period. Records of compliance checks were also lacking. For example, there was no record of the regular compliance check for the first seven months of 2015, and the results for the review of tape recording was not documented prior to September 2015. The effectiveness of the compliance checks was thus called into question.

23. China Rise's failure to maintain proper records of order placing instructions and its compliance checks was in breach of:

    (a) paragraph 3.9(b) of the Code of Conduct, which requires a licensed person to use a telephone recording system to record instructions received from clients through the telephone and maintain telephone recordings as part of its records for at least six months; and

    (b) paragraph 6 of Part IV and paragraph 6 of Part VII of the Internal Control Guidelines, which require the management of a licensed corporation to establish and maintain:

        (i) effective record retention policies which ensure that all relevant legal and regulatory requirements are complied with and which enable the firm and the SFC to carry out comprehensive reviews or investigations; and

        (ii) policies and procedures which ensure that clear and comprehensive audit trails are created to precisely record all orders from the time of origination, including the time the order was received or initiated, through order execution and settlement.

Conclusion

24. Having considered all relevant circumstances, the SFC is of the opinion that China Rise has been guilty of misconduct, and its internal control failures and regulatory breaches set out above have called into question its fitness and properness to remain a licensed corporation.

25. In deciding the disciplinary sanction set out in paragraph 1, the SFC has had regard to its Disciplinary Fining Guidelines and has taken into account all relevant circumstances, including:

(a) Shiu placed 199 short selling orders in breach of section 170 of the SFO over a period of five months (and was convicted of 14 charges of illegal short selling) and China Rise failed to detect and prevent any of them;

(b) China Rise failed to stop Shiu from continuing his illegal short selling activities even after HKEx made enquiries;

(c) the ROs responsible for monitoring staff dealings were derelict in their duties and blatantly disregarded China Rise's internal policies regarding conflicts of interest;

(d) Shiu and the RO responsible for monitoring his dealings have left China Rise;

(e) China Rise has taken steps to remediate some of the above internal control deficiencies, such as revising its written policies to restrict the use of the MWS by its staff and prohibit cross trades between staff members and clients;

(f) China Rise had not gained any profit from the above matters;

(g) China Rise cooperated with the SFC in accepting the SFC's findings and resolving the disciplinary proceedings; and

(h) China Rise has an otherwise clean disciplinary record.