

## SFC reprimands and fines ICBC International Capital Limited and ICBC International Securities Limited \$12.5 million each for failures related to IPO shares subscription

21 May 2014

The Securities and Futures Commission (SFC) has reprimanded ICBC International Capital Limited (ICBCI Capital) and ICBC International Securities Limited (ICBCI Securities) (collectively ICBCI) and fined them \$12.5 million respectively in relation to their role in the initial public offering of Powerlong Real Estate Holdings Limited (Powerlong) in 2009 (Notes 1, 2, 3 & 4).

An SFC investigation into the practice and procedure adopted by ICBCI found that it had:

- failed to conduct customer due diligence and perform ongoing scrutiny of accounts of certain placees referred by Powerlong (Placees) to ensure that the transactions being conducted were consistent with its knowledge of the Placees, taking into account their source of funds (Note 5);
- turned a blind eye to the lack of independence of Placees for the subscription of Powerlong's shares allotted through its listing (the Offer Shares) on The Stock Exchange of Hong Kong Limited (SEHK);
- facilitated the listing of Powerlong by ensuring that margin financing would be extended to the Placees despite its suspicion of their non-independence; and
- failed to use reasonable efforts to ensure that submissions to the SEHK were true, accurate and not misleading.

An SFC investigation revealed that the Placees were referred by Powerlong to ICBCI Capital, which in turn referred them to its affiliate ICBCI Securities to open accounts for the subscription of the Offer Shares. ICBCI Securities accepted the subscriptions of the Placees without conducting know-your-client due diligence as required under the Code of Conduct to either ascertain their financial situation or confirm their independence from Powerlong (Note 6).

The Offer Shares were subsequently re-priced due to insufficient demand. Upon the request of Powerlong, ICBCI Capital informed ICBCI Securities that extensive margin financing would have to be extended to particular Placees so that subscriptions under their accounts could be increased to prevent the listing from falling through.

Thereafter, subscriptions of these Placees suddenly increased by as much as tenfold. ICBCI Securities failed to perform ongoing scrutiny to ensure that the Placees' subscriptions were consistent with its knowledge of their financial situation.

In light of the unusual and substantial increase in subscription sizes of these Placees, a certain staff member of ICBCI Capital voiced out his suspicion that the orders of these Placees belonged to Powerlong. However, no inquiry was made by ICBCI Capital to ascertain whether this was the case or the relationship between the Placees and Powerlong. Although the subscriptions of some of these Placees far exceeded their declared net worth, ICBCI Capital nevertheless allocated the Offer Shares to them. As a result, massive debit balances were triggered after the Offer Shares were booked into their accounts. Margin financing of as much as 50%, which was not generally granted in international primary placings, was then extended by ICBCI Securities to certain Placees.

When some Placees raised questions regarding third-party settlement of their subscriptions, instead of questioning the reasons behind them, personnel of ICBCI Securities advised them to settle their allotment by various methods which ensured that the identity of the third-party depositors could not be traced.

ICBCI Securities filed the Marketing Statement (known as Form D) and a letter vouching placee independence with the SEHK even though it had not received all independence confirmations from the Placees at the time of making the filing with the SEHK in October 2009. ICBCI Capital filed a Sponsor's Declaration (known as Form E) to the SEHK without making any reasonable enquiries that the number of Offer Shares in public hands would satisfy the minimum percentage prescribed by Rule 8.08 of the Listing Rules (Note 7).

The SFC took into account that ICBCI has an otherwise clean record and acknowledges ICBCI's cooperation to address the SFC's concerns. ICBCI has agreed to accept the disciplinary action and has committed to engage a firm of independent reviewers to undertake a comprehensive review of its systems and controls and to implement the recommendations made by the reviewer to the satisfaction of the SFC.

Mr Mark Steward, the SFC's Executive Director of Enforcement, said, "These failings go to the heart of the sponsor's obligation to help ensure the integrity of the initial public offering market. The sponsor is the principal responsible for the management of the listing process and these failings cannot be placed at the foot of any other person."

End

Notes:

1. ICBCI Capital is licensed under the Securities and Futures Ordinance (SFO) to carry on Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities.
2. ICBCI Securities is licensed under the SFO to carry on Type 1 (dealing in securities) regulated activity.
3. ICBCI Capital was one of the joint sponsors and bookrunners; and ICBCI Securities was one of the joint lead managers.
4. Powerlong was listed on the Main Board of The Stock Exchange of Hong Kong Limited in 2009.
5. "Placees" refers to investors who subscribed for the offer shares via the international tranche.
6. Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission
7. Rule 8.08(1)(a) of Main Board Listing Rules of the SEHK prescribes that an open market in the securities for which listing is sought means that at least 25% of the issuer's total issued share capital must at all times be held by the public.
8. A copy of the [Statement of Disciplinary Action](#) in relation to the matter is available on the SFC website.

Page last updated : 21 May 2014

---

## STATEMENT OF DISCIPLINARY ACTION

---

### The Disciplinary Action

1. The Securities and Futures Commission (SFC) has taken the following disciplinary action against ICBC International Capital Limited<sup>1</sup> (ICBCI Capital) and ICBC International Securities Limited<sup>2</sup> (ICBCI Securities):
  - (a) publicly reprimanded ICBCI Capital and ICBCI Securities (collectively, ICBCI), pursuant to section 194(1)(b)(iii) of the Securities and Futures Ordinance (SFO); and
  - (b) imposed a financial penalty in the sum of \$12.5 million on each of ICBCI Capital and ICBCI Securities, pursuant to section 194(2)(b) of the SFO.

### Summary of facts

2. In light of an **anonymous complaint which alleged** that ICBCI Capital, one of the joint sponsors and bookrunners in the listing of Powerlong Real Estate Holdings Limited (Powerlong) in 2009, and ICBCI Securities, one of the joint lead managers in such listing, had **procured nominee accounts to subscribe for shares allotted through Powerlong's listing and that such subscriptions were financed by Powerlong**, the SFC conducted an investigation into the process adopted by ICBCI in underwriting such shares (the Offer Shares).
3. The SFC's investigation reveals that:
  - (a) ICBCI Capital had:
    - (i) not only turned a blind eye to the lack of independence of certain placees referred by Powerlong (Placees) but also facilitated the listing of Powerlong by ensuring that margin financing would be extended to such Placees by ICBCI Securities despite its suspicion of their non-independence; and
    - (ii) failed to use reasonable efforts to ensure that the information and representations it provided to The Stock Exchange of Hong Kong Limited (SEHK) were true, accurate and not misleading by falsely declaring in the Sponsor's Declaration (Form E) that, having made

---

<sup>1</sup> ICBCI Capital is a corporation licensed to carry on business in Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities.

<sup>2</sup> ICBCI Securities is a corporation licensed to carry on business in Type 1 (dealing in securities) regulated activity.

all reasonable enquiries, 25% of the total issued share capital of Powerlong would be held in the hands of the public, in accordance with rule 8.08 of the Listing Rules<sup>3</sup>,

in breach of General Principle (GP) 2 of the Code of Conduct<sup>4</sup>;

(b) ICBCI Securities had:

(i) failed to conduct customer due diligence and perform ongoing scrutiny of accounts of Placees to ensure that the transactions being conducted were consistent with its knowledge of them, taking into account their source of funds, in breach of GP 4 and paragraph 5.1 of the Code of Conduct as well as paragraphs 6.1.1 and 6.1.2 of the AML Guidance Note<sup>5</sup>;

(ii) not only turned a blind eye to the lack of independence of Placees but also facilitated Powerlong's listing by extending margin financing to them despite the existence of various matters which tend to show their non-independence, without:

1. ensuring that the Placees had the financial capacity to meet obligations arising from instructions they gave prior to extending margin financing to them in accordance with paragraph 3 of Schedule 5 of the Code of Conduct; and

2. satisfying itself on reasonable grounds that instructions for subscription of Offer Shares originated from the Placees in accordance with paragraph 5.4 of the Code of Conduct,

in breach of GP2 of the Code of Conduct; and

(iii) failed to ensure that all independence confirmations were received from Placees before submitting the Marketing Statement (Form D) dated 5 October 2009 declaring that none of the Offer Shares had been placed with the nominees of Powerlong's directors or their associates or any existing shareholder in accordance with rule 5 in Appendix 6 of the Listing Rules, in breach of GP2 of the Code of Conduct.

#### Failing to conduct customer due diligence and perform ongoing scrutiny

4. GP4 and paragraph 5.1 of the Code of Conduct provide that a licensed corporation should take all reasonable steps to seek information and establish from its clients their financial situation, investment experience and investment objectives.

---

<sup>3</sup> Rules Governing the Listing of Securities on the SEHK.

<sup>4</sup> The Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

<sup>5</sup> Prevention of Money Laundering and Terrorist Financing Guidance Note

5. The ICBCI Group<sup>6</sup> Compliance Manual contained relevant provisions regarding the obtaining of such information from clients. Staff members of ICBCI Securities were expected to take reasonable steps to ensure that know-your-client requirements (KYC) in respect of clients of the ICBCI Group are satisfied when opening client accounts.
6. Notwithstanding the above requirements, a number of former staff members of ICBCI Securities considered that since **the Placees, who were friends and families introduced by Powerlong**, were referred by ICBCI Capital, ICBCI Capital should have been satisfied with the background of such Placees before referring them to ICBCI Securities. Conversely, former staff members of ICBCI Capital considered that it was the responsibility of ICBCI Securities to ensure that the KYC requirements of the Placees had been fulfilled. As a result, **no KYC checks of the Placees were conducted by either ICBCI Securities or ICBCI Capital**.
7. Further, none of the responsible account executives of ICBCI Securities were aware of either the regulatory requirements or the requirement set out in the Compliance Manual to obtain information in respect of a client's financial situation, investment experience and investment objectives. As a result, no such information was obtained.
8. Due to insufficient demand, the Offer Shares were re-priced. Upon Powerlong's request, ICBCI Capital informed ICBCI Securities that the level of margin financing would have to be increased so that the subscription sizes of such Placees could be boosted in order to prevent Powerlong's listing from falling through. **A member of senior management from Powerlong subsequently informed a staff member of ICBCI Capital that subscriptions would be increased via four accounts. Consequently, orders of four Placees suddenly surged by as much as tenfold.**
9. It was apparent that such subscriptions far exceeded the declared net worth of the Placees. However, personnel of ICBCI Securities failed to perform ongoing scrutiny of the transactions in these Placees' accounts. Further, various former staff members of ICBCI Securities took the view that the Placees may not necessarily be allocated with the number of Offer Shares which they have subscribed for. **As it turned out, some Placees were allocated with Offer Shares in an amount of up to a possible 127 times their declared net worth.**
10. Without having conducted KYC checks or ascertained clients' financial situation which was in breach of the Compliance Manual as well as GPs 2 and 4 and paragraph 5.1 of the Code of Conduct, subscriptions for Offer Shares under the names of clients, including the Placees were accepted by ICBCI Securities.

Turning a blind eye to the lack of independence of Placees and extending margin financing to them

11. Not only did Powerlong refer the Placees to ICBCI Capital which made arrangements with ICBCI Securities to open accounts for them for the subscription of Offer Shares, it had also been actively involved in updating

---

<sup>6</sup> The ICBCI Group comprises various entities, including but not limited to ICBCI Capital and ICBCI Securities.

ICBCI Capital on the size of the Placees' orders. Various personnel of Powerlong had, among other things:

- (a) liaised with ICBCI Capital in relation to the increase of the orders of these Placees; and
  - (b) requested ICBCI Capital that margin financing of 50% be provided to some of the Placees so that their subscription sizes could be increased to prevent the listing of Powerlong from falling through.
12. After the sudden increase in subscriptions of the four strategic Placees, a responsible officer (RO) of ICBCI Capital suspected that there were issues of independence of some of the Placees and escalated the same to his supervisor, who was also an RO of ICBCI Capital. However, no follow-up action was taken to ascertain the independence of the Placees.
  13. It was apparent that some of the Placees lacked the financial capability to settle their allocation of Offer Shares since their subscriptions and allocations were greater than their declared net worth. Nevertheless, Offer Shares were booked into accounts under their names which triggered massive debit balances. No prior approval for limit excess was obtained when the Offer Shares were booked into the accounts of the Placees.
  14. When deposits were made in settlement of their allocations, none of the then staff members of ICBCI Securities questioned the source of funds of the Placees. In fact, in order to circumvent the internal policies on third party transactions, personnel of ICBCI Securities at times advised them to make payment by way of cash or cashier's orders so that the identity of the third party depositor could not be traced.
  15. There were also indications from various telephone recordings between personnel of ICBCI Securities on one hand, and the Placees / persons contacting personnel of ICBCI Securities on behalf of the Placees on the other, that some of the Placees were suspected to be financially dependent on Powerlong and/or its management / controlling shareholders. However, no inquiry as to their independence was made.
  16. Subsequent to the final allocation of Offer Shares, upon the request of ICBCI Capital, high levels of margin financing were sought by ICBCI Securities on behalf of such the Placees which were not generally available to clients in international primary placings. Margin financing at a ratio of as high as 50% was extended by ICBCI Securities to the four strategic Placees despite the fact that approval from senior management was not obtained.
  17. In light of the above, despite the existence of the hallmarks which tend to show that the Placees were relying upon Powerlong for financial assistance in the subscription of Offer Shares, ICBCI Capital chose to turn a blind eye to the lack of independence of the Placees, contrary to GP2 of the Code of Conduct. Further, ICBCI Securities could not have been satisfied on reasonable grounds as to the identity of the person ultimately responsible for originating the instruction at the time of the transaction and the instruction given by such person, which is in breach of paragraphs 6.1.1 and 6.1.2 of the AML Guidance Note.

Failing to ensure that all independence confirmations were received from Placees before submitting the Marketing Statement to the SEHK

18. Rule 9.11(35) of the Listing Rules requires the lead broker to file a Marketing Statement (Form D) and a placee list with the SEHK, confirming, among other things, the number of placees, the number of shares placed and the independence of the placee.
19. In accordance with rule 9.11(35) of the Listing Rules, ICBCI Securities filed a Marketing Statement (Form D) on 5 October 2009.
20. In fact, the Marketing Statement and a letter vouching placee independence were filed by ICBCI Securities with the SEHK even though it had not received independence confirmations from all of the Placees at the time of filing.
21. Given the findings, the SFC is of the view that ICBCI Securities failed to ensure that all independence confirmations were received from Placees before submitting the Marketing Statement to the SEHK declaring that none of the Offer Shares had been placed with the nominees of Powerlong's directors or their associates or any existing shareholder, in breach of GP2 of the Code of Conduct.

Submitting information and representations to the SEHK without using reasonable efforts to ensure that the same was true, accurate and not misleading

22. Rule 9.11(36) of the Listing Rules requires the sponsor to file a Sponsor's Declaration (Form E) confirming that at least 25% of the issuer's share capital are held by the public before the commencement of dealings in shares.
23. In accordance with rule 9.11(36) of the Listing Rules, ICBCI Capital filed a Sponsor's Declaration (Form E) on 13 October 2009.
24. A former RO of ICBCI Capital admitted that he relied on the clearance of the allotment results announcement by SEHK, wherein it was stated that the minimum public float requirement had been met, before signing off the Sponsor's Declaration to confirm the same. In short, ICBCI Capital did not take any steps to ascertain whether such requirement as prescribed by Rule 8.08 of the Listing Rules had indeed been complied with.
25. Given the findings, the SFC is of the view that ICBCI failed to use reasonable efforts to ensure that the information and representations it provided to the SEHK were true, accurate and not misleading before filing the Sponsor's Declaration.

**Conclusion**

26. Having considered all the circumstances, the SFC is of the opinion that ICBCI is guilty of misconduct and/or not a fit and proper person to remain licensed given its failure to take adequate steps to comply with the relevant provisions of the Code of Conduct and the Listing Rules.

27. A breakdown of the fine in paragraph 1(b) is as follows:
- (a) \$7,500,000 for the failure as summarised in paragraph 3(a)(i) above;
  - (b) \$5,000,000 for the failure as summarised in paragraph 3(a)(ii) above;
  - (c) \$1,500,000 for the failures as summarised in paragraph 3(b)(i) above;
  - (d) \$7,500,000 for failures as summarised in paragraph 3(b)(ii) above; and
  - (e) \$3,500,000 for the failure as summarised in paragraph 3(b)(iii) above.
28. In coming to the decision to take disciplinary action set out in paragraph 1 against ICBCI Capital and ICBCI Securities for the matters put forward in paragraph 3 above, the SFC has:
- had regard to the SFC Disciplinary Fining Guidelines;
  - taken into account:
    - ICBCI's co-operation with the SFC
    - that ICBCI has committed to engage a firm of independent reviewers to undertake a comprehensive review its systems and controls and to implement the recommendations made by the reviewer to the satisfaction of the SFC
    - that ICBCI has no previous disciplinary record; and
  - decided that the sanction of public reprimand and fine is most appropriate and commensurate with the gravity of the relevant regulatory breaches.