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## SFC reprimands and fines JS Cresvale Securities HK\$2.5 million

26 Mar 2015

The Securities and Futures Commission (SFC) has reprimanded and fined JS Cresvale Securities International Limited (JS Cresvale Securities) HK\$2.5 million over serious deficiencies in relation to its sale of two unlisted investment products involving US\$99 million between 2008 and 2010 (Note 1).

The disciplinary action followed an SFC investigation which found serious deficiencies in JS Cresvale Securities' systems and controls for ensuring the suitability of the recommendations or solicitations it made to clients when selling the two products, namely, 浩騰科技信用連結債券 and 浩騰11海外可轉換公司債. The products were recommended and sold to 59 clients in 2008, 26 clients in 2009 and 4 clients in 2010.

Specifically, the SFC found that JS Cresvale Securities:

- did not conduct any product due diligence or risk assessment on the products;
- did not have complete risk profiles of its clients as no steps were taken to assess the clients' risk tolerance levels;
- had no systems and controls to guide its representatives to conduct proper suitability assessment when selling the products; and
- did not maintain documentary records of the investment advice or recommendations given to its clients nor provide clients with a copy of the written advice.

In determining the penalty, the SFC took into account that:

- JS Cresvale Securities co-operated in resolving the disciplinary proceedings;
- it agreed to conduct an independent review of its systems and controls for distribution of unlisted investment products and to enhance its complaint handling procedures; and
- there is no evidence of client loss suffered from its distribution of the two unlisted products.

End

Note:

1. JS Cresvale Securities is licensed under the Securities and Futures Ordinance (SFO) to carry on Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities. JS Cresvale Securities' licence for Type 2 (dealing in futures contracts) regulated activity has been suspended since September 2014.

[A copy of the Statement of Disciplinary Action is available on the SFC website](#)

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## STATEMENT OF DISCIPLINARY ACTION

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### The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has publicly reprimanded and fined JS Cresvale Securities International Limited (**JS Cresvale Securities**)<sup>1</sup> \$2.5 million pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).
2. The disciplinary action is taken because JS Cresvale Securities had failed to:
  - (a) ensure adequate product due diligence had been conducted on unlisted investment products before making recommendations or solicitations to its clients for them to invest in the products;
  - (b) ensure that the recommendations or solicitations made to its clients were suitable for and reasonable in all the circumstances of each of its clients in the distribution of unlisted investment products; and
  - (c) maintain proper documentary records of the investment advice or recommendations given to its clients and provide clients with a copy of the written advice.

### Summary of facts

3. Between 2008 and 2010, JS Cresvale Securities recommended or solicited the sale of two unlisted products<sup>2</sup>, 浩騰科技信用連結債券 and 浩騰 11 海外可轉換公司債 (Wonten 11 (5364 TT) CB 0% 3-year Term ECB) (collectively "**Products**"), to its clients and recorded an aggregate transaction amount of approximately US\$99 million from the sale of the Products. The Products were recommended and sold to 59 clients in 2008, 26 clients in 2009 and 4 clients in 2010.

### *Regulatory requirements*

4. General Principle 2 (diligence), paragraphs 3.4 (advice to clients: due skill, care and diligence) and 5.2 (know your client: reasonable advice) of the Code of Conduct<sup>3</sup> require a licensed corporation to ensure that, through the exercise

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<sup>2</sup> Excluding insurance and investment-linked assurance schemes, i.e. ILAS products

<sup>3</sup> Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission

of due diligence, its investment recommendations to clients are based on thorough analysis and are reasonable in all the circumstances.

5. Paragraph VII(3) of, and paragraph 3 of the Appendix to, the Management Guidelines<sup>4</sup> provide that a licensed corporation in the business of offering investment advice should take steps to document and retain the reasons for its recommendations or advice given to the client and to implement special procedures to document (and provide a copy to the client) the rationale underlying investment advice rendered or recommendations made.

#### *Product due diligence*

6. The SFC found that between 2008 and 2010, JS Cresvale Securities did not take necessary steps to acquire an adequate understanding of the nature and risks of the Products. It admitted that it did not have the applicable procedures in place for performing due diligence on the Products. It started to undertake due diligence on investment products in the 4<sup>th</sup> quarter of 2010 and had no relevant and written policy and procedure between 2004 and 2010.
7. Without conducting due diligence and risk assessment of the Products and having in place proper policy to give relevant guidance to its staff on the exercise, JS Cresvale Securities and its licensed representatives would not have been able to:
  - (a) ensure that they had sufficient understanding of the nature and risks of the Products for determining for which types of clients the Products would have been suitable, before any recommendation was made; and
  - (b) explain to each client thoroughly the Products' nature and risk to enable the client to make informed investment decisions.
8. JS Cresvale Securities' failures to conduct product due diligence of the Products between 2008 and 2010 and have relevant policy in place made it impossible for it to adequately discharge its suitability obligations as prescribed in paragraphs 3.4 and 5.2 of the Code of Conduct. Such failures show that JS Cresvale Securities did not act with due skill, care and diligence, and in the best interests of its clients as required under General Principle 2 of the Code of Conduct.

#### *Suitability of recommendations*

9. JS Cresvale Securities only commenced to undertake suitability assessment in the 1<sup>st</sup> quarter of 2011 and had no guidance and procedures in place for determining suitability of products before March 2011.
10. Apart from its failure to conduct product due diligence on the Products, JS Cresvale Securities only started to take steps to collect from its clients information on their risk tolerance and assess its clients' risk tolerance levels in around March 2011. No relevant and written policy and procedure were in place before March 2011.

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<sup>4</sup> Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC

11. The deficiencies in JS Cresvale Securities' systems and controls had made it impossible for JS Cresvale Securities to provide reasonably suitable recommendations by matching the risk return profile of the Products with the personal circumstance of each relevant client between 2008 and 2010. Moreover, JS Cresvale Securities' advice and recommendations would not have been based on thorough analysis in the circumstances.
12. The lack of guidance and proper system for conduct of suitability assessment means that account executives ("AE") of JS Cresvale Securities were left to assess what products could be sold to the clients based on their own criteria. This casts serious doubt that any suitability assessment by its AEs, if conducted at all, could have been properly done in the circumstances.
13. In addition, JS Cresvale Securities failed to put in place any written guidelines and controls to ensure that it had provided all relevant material information to its clients regarding the Products.
14. All in all, the deficiencies in JS Cresvale Securities' systems and controls for ensuring suitability of the Products to its clients when recommending or soliciting the sale of the Products to the clients between 2008 and 2010 demonstrate JS Cresvale Securities' failure to adequately discharge its regulatory duty under General Principle 2 and paragraphs 3.4 and 5.2 of the Code of Conduct.

*Documentation of investment advice and recommendations*

15. JS Cresvale Securities confirmed in the SFC's investigation that it had no documentation of its investment advice or recommendations made to its clients and had no relevant policy and procedure in place between 2004 and 2012.
16. Record of communications with clients to whom JS Cresvale Securities had recommended or solicited the sale of the Products between 2008 and 2010 was also not available.
17. The evidence suggests that JS Cresvale Securities has failed to keep documentary records of its investment recommendations or advice given to clients who purchased the Products in accordance with the Management Guidelines. In addition, JS Cresvale Securities had no policies and procedures for ensuring that it properly discharged its duty in relation to the documentation of advice given to its clients.
18. Without having the investment recommendations or advice documented, JS Cresvale Securities would not have been able to effectively supervise and monitor its AEs to ensure that the recommendations or solicitations they made to the clients were suitable and reasonable in all the circumstances in accordance with its regulatory duty under the Code of Conduct.
19. JS Cresvale Securities' failures to maintain proper documentary records of the investment advice or recommendations given to its clients and provide clients with a copy of the written advice constitute breaches of General Principle 2 of the Code of Conduct and paragraph VII(3) of, and paragraph 3 of the Appendix to, the Management Guidelines.

## **Conclusion**

20. Intermediaries in making investment recommendations or solicitations to clients are required to comply with the suitability obligations under the Code of Conduct. Failure to do so could lead to mis-selling of investment products. JS Cresvale Securities' controls and procedures were seriously deficient and prejudicial to the interest of its clients.