

## STATEMENT OF DISCIPLINARY ACTION

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### The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has reprimanded and fined Ample Capital Limited (**ACL**)<sup>1</sup> HK\$5.5 million pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).
2. The disciplinary action is taken in respect of ACL's failure to discharge its duties as a sole sponsor in the listing application (**Listing Application**) of COCCI International Limited (**COCCI**) on the Growth Enterprise Market (**GEM**) of The Stock Exchange of Hong Kong Limited (**SEHK**), in that ACL has failed to:
  - (a) perform all reasonable due diligence on COCCI before submitting the Listing Application, by failing to:
    - (i) conduct adequate due diligence on suspicious cash settlements made by a major wholesale distributor (**Distributor**) to COCCI through third parties and keep proper records of its due diligence work;
    - (ii) ascertain the background and independence of the Distributor and its associates;
    - (iii) assess the reasonableness of COCCI's sales to the Distributor; and
  - (b) critically assess the reliability of the shipping documents provided by COCCI before relying on them as part of its due diligence.
3. The SFC has also suspended the licence of Tang Ho Wai Howard (**Tang**) for 17 months from 15 October 2021 to 14 March 2023 for failing to discharge his duties as a responsible officer and sponsor principal of ACL in charge of supervision of the execution of the Listing Application<sup>2</sup>.

### Summary of facts

#### *Background*

4. COCCI together with its subsidiaries (collectively, the **Group**) engaged in the design, marketing, retail sales and distribution of ladies-wear products under its self-owned brand "COCCI".
5. The Group's revenue for the year ended 31 December 2015 was almost double that for the year ended 31 December 2014 primarily due to the sales of out-of-season products at a discount to the Distributor, which re-distributed COCCI's products mainly to Saudi Arabia. Its sales to the Distributor accounted for 50.2% and 23.3% of COCCI's total revenue for the year ended 31 December 2015 and the four months ended 30 April 2016.

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<sup>1</sup> ACL is licensed under the SFO to carry on Type 1 (dealing in securities), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities.

<sup>2</sup> Tang has been approved by the SFC to act as a responsible officer of ACL in respect of its Type 6 (advising on corporate finance) and Type 1 (dealing in securities) regulated activities since 22 May 2007 and 2 September 2020 respectively. Tang has also been approved to act as a sponsor principal of ACL since 11 February 2010.

6. On 31 January 2016, COCCI appointed ACL as its sole sponsor. On 6 September 2016, ACL submitted the listing application (**First Application**) for COCCI together with the Application Proof prospectus to SEHK.
7. Between October 2016 and March 2017, the SFC and SEHK made various comments on, among other things, COCCI's wholesale business.
8. Due to a lapse of more than six months from the First Application, COCCI re-submitted a listing application on 18 April 2017 (**Second Application**). ACL continued to act as its sole sponsor.
9. The SFC and SEHK made further comments following the submission of the Second Application, including through two letters both dated 9 June 2017. The SFC and SEHK were of the view that the revised prospectus submitted by COCCI still failed to explain and provide sufficient information on various aspects of COCCI's wholesale business (**Comments**).
10. ACL did not respond to the Comments. The Second Application lapsed on 17 October 2017.

*Inadequate due diligence on suspicious cash settlements*

11. Between March 2016 and June 2016, a total of 24 deposits (totaling RMB9,715,000) were made by five third parties (**Third Parties**) to a Mainland bank account of the Group to settle payments owed by the Distributor to the principal operation branch of the Group in the Mainland (**Mainland Branch**).
12. ACL learnt from COCCI's directors that:
  - (a) the sole shareholder and director of the Distributor (**Ms A**) has made cash settlements in Hong Kong dollar to the Mainland Branch on behalf of the Distributor in the following manner:
    - (i) COCCI's chairman would specify one or more of the Third Parties as recipient(s) of cash settlements by Ms A; and
    - (ii) the cash settlements would be made at meeting venues agreed between Ms A and COCCI's chairman or the Third Parties.
  - (b) After receiving the cash settlements from Ms A, the Third Parties would convert them into Renminbi and physically carry the cash to the Mainland and deposit it into the Mainland Branch's bank account.
  - (c) The reason for the arrangement were that the Mainland Branch did not maintain bank accounts in Hong Kong for receiving the cash settlement from Ms A directly, and settlements from the Distributor to the Mainland Branch were subject to foreign exchange control regulations in the Mainland.
13. Settlement of payments through third parties by a customer is a red flag as third party payments might be used to disguise the original source of funds and facilitate a fraudulent scheme. This is particularly so in this case as one of the Third Parties was an employee of COCCI's major supplier.

14. However, ACL failed to critically assess the reasons behind the third party cash settlement arrangement, nor did it conduct any independent due diligence to ascertain the truth and completeness of COCCI's representations in this respect.
15. ACL also failed to maintain any records to demonstrate the due diligence it conducted, including its alleged discussions with COCCI's directors and reporting accountants regarding the third party cash settlement arrangement.

*Failure to ascertain the background and independence of the Distributor and its associates*

16. ACL was aware that the Distributor's business activities were carried out by its sole shareholder (Ms A) and members of staff from her jewellery company.
17. Although there was information suggesting a connection between Ms A's jewellery company and COCCI, for example:
  - (a) one of the co-owners of the jewellery company was a company solely owned by an indirect shareholder (**Mr X**) of COCCI; and
  - (b) one of its directors (**Mr Y**) was also a director of COCCI's major supplier, as well as a director and sole shareholder of a company which is a franchisee of COCCI and a management agent of certain self-operated retail outlets of COCCI,

ACL failed to undertake any additional due diligence to ascertain Mr X's and Mr Y's involvement in the Distributor's business activities, and verify the independence of the Distributor or its sole shareholder, Ms A, from COCCI and its supplier.

*Failure to assess the reasonableness of COCCI's sales to the Distributor*

18. Since the Group's revenue in 2015 rose significantly as a result of its sales to the Distributor and a substantial portion of COCCI's products was allegedly ultimately sold to end customers in Saudi Arabia via the Distributor, it was imperative for ACL to conduct adequate due diligence to assess the reasonableness of such sales<sup>3</sup>.
19. However, ACL had performed minimal due diligence regarding the sales of COCCI's products in Saudi Arabia before submission of the Listing application. While ACL had attended a telephone interview (conducted by COCCI's reporting accountants) with a major Saudi Arabian customer of the Distributor<sup>4</sup>, ACL did not seek to obtain any objective data to verify information provided by the customer, nor did it conduct any independent search on the customer's background and scale of operations in Saudi Arabia.
20. It was only after ACL received comments from the SFC/SEHK after submission of the First Application that it performed further due diligence, such as interviewing the Saudi Arabian customer and visiting its retail stores in Saudi Arabia.

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<sup>3</sup> The SEHK's Guidance Letter GL36-12 (May 2012) on "Distributorship business model – risks and disclosure in listing documents" stipulates that sponsors are expected to have performed sufficient due diligence work in relation to the fairness and reasonableness of sales to distributors recorded during the track record period. The Guidance Letter highlighted the risk of channel stuffing in a distributorship business model and states that, "[w]hile a sharp increase in sales during the track record period may indicate a vibrant business, there is a risk that these are artificially pumped-up sales unsustainable by an actual rise in demand from ultimate end-users".

<sup>4</sup> According to ACL, a majority (estimated to be over 80% in 2015 and 100% in the four months ended 2016) of COCCI's products sold to the Distributor were re-distributed to this customer in Saudi Arabia.

*Failure to critically assess the reliability of the shipping documents provided by COCCI*

21. ACL obtained from COCCI a total of 25 sets of shipping documents in relation to the shipment of COCCI's products from the Distributor to the Saudi Arabian customer.
22. However, it did not critically assess the reliability of the shipping documents before relying on them as part of its due diligence.
23. It also failed to identify the red flags which cast doubt on the reliability of shipping documents, for instance:
  - (a) the container identification number was marked as "ABCD/111111/TBA" in all 25 sets of bills of lading in the shipping documents; and
  - (b) the dates shown in most of the bills of lading do not match with the sailing schedules of the relevant vessels/voyages that could be found in publicly available sources.

**Conclusion**

24. Having considered all relevant circumstances, the SFC is of the view that ACL has breached:
  - (a) General Principle 2 (Diligence) of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (**Code of Conduct**) and paragraph 5.1 (Due skill and care) of the Corporate Finance Adviser Code of Conduct by failing to act with due skill, care and diligence and observe proper standards of market conduct, in the best interests of its clients and the integrity of the market.
  - (b) Paragraphs 17.2(b) and 17.4(a) (Reasonable due diligence) of the Code of Conduct by failing to complete all reasonable due diligence on COCCI before submitting the Listing Application.
  - (c) Paragraph 17.6(a) (Reasonable judgment) of the Code of Conduct by failing to exercise reasonable judgment on the nature and extent of due diligence work needed in relation to COCCI having regard to all relevant facts and circumstances.
  - (d) Paragraph 17.6(b) (Professional scepticism) of the Code of Conduct and paragraph 2 of PN2<sup>5</sup> by failing to examine with professional scepticism the accuracy of information provided by COCCI and be alert to information that contradicted or brought into question the reliability of such information.
  - (e) Paragraph 17.6(c) (Appropriate verification) of the Code of Conduct by failing to undertake additional due diligence to ascertain the truth and completeness of the information provided by COCCI, after ACL became aware of circumstances that could cast doubt on the information provided to it or otherwise indicated a potential problem or risk.
  - (f) Paragraph 17.6(e) (Independent due diligence steps) of the Code of Conduct by failing to conduct independent due diligence steps to inquire directly of

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<sup>5</sup> Practice Note 2 to the Rules Governing the Listing of Securities on GEM of SEHK.

knowledgeable persons within or outside the listing applicant and in relation to material matters, independently obtain information from sources outside the listing applicant.

- (g) Paragraphs 17.2(e) and 17.10 (Proper records) of the Code of Conduct by failing to maintain proper records relating to the due diligence performed (together with its results) in respect of the Listing Application so as to demonstrate to the SFC its compliance with the Code of Conduct.
25. The SFC considers that ACL's failures are attributable to Tang's failure to discharge his duties as a sponsor principal, a responsible officer and a member of the senior management of ACL, in that he has failed to:
- (a) exercise due skill, care and diligence in handling the Listing Application;
  - (b) diligently supervise the transaction team to carry out the sponsor work undertaken by ACL in respect of the Listing Application; and
  - (c) ensure the maintenance of appropriate standards of conduct by ACL.
26. In reaching the decision to take the disciplinary actions set out in paragraphs 1 and 3 above, the SFC has taken into account all relevant circumstances of this case, including:
- (a) substandard due diligence work of sponsors could assist the listing of companies that are, in fact, not suitable for listing;
  - (b) as the Listing Application had lapsed, no harm has been caused to members of the investing public;
  - (c) the SFC has previously issued two compliance advice letters to ACL in respect of its conduct as a sponsor in two separate listing applications, which should have put it on heightened alert of the need to improve its due diligence work;
  - (d) ACL has no previous disciplinary record with the SFC;
  - (e) ACL's financial situation; and
  - (f) ACL and Tang cooperated with the SFC in resolving the SFC's concerns.