

STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has publicly reprimanded and fined Ruifeng Securities Limited (**RSL**)¹ HK\$5.2 million pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).
2. The disciplinary action is taken in relation to RSL's failures and breaches relating to its fund management activities and account opening procedures.
3. The SFC has also suspended the licence of Fang Zhi (**Fang**) for 10 months from 1 December 2023 to 30 September 2024 for failing to discharge his duties as a responsible officer (**RO**) of RSL in charge of its fund management activities².

Summary of Facts

A. Deficiencies in RSL's management of a Cayman-incorporated fund (Fund)

4. By an investment management agreement dated 12 April 2019, RSL was appointed as the investment manager of the Fund. Fang has been the RO at RSL primarily responsible for handling and managing the Fund, including selecting and deciding on the investments for the Fund.
 5. The Fund commenced operation on 5 August 2019. As at 29 May 2020:
 - (a) about 90% of the Fund's net asset value (**NAV**)³ was invested in fixed income products guaranteed by or linked to a company (a property developer) in Mainland China (**Company**); and
 - (b) over 98% of the shares in the Fund were held by one investor (**Investor A**)⁴.
 6. Following an investigation, the SFC has identified various deficiencies in RSL's management of the Fund as set out in sections A1 to A4 below.
- #### A1. Failure to identify, prevent, manage and minimise the conflict of interest arising from its underwriting activities and disclose the conflict to the Fund's investors
7. On 9 September 2019, RSL entered into a purchase agreement (**Purchase Agreement**) to purchase US\$40 million of senior notes issued by a special

¹ RSL is licensed to carry on Type 1 (dealing in securities), Type 4 (advising on securities) and Type 9 (asset management) regulated activities under the SFO.

² Fang has been approved by the SFC to act as an RO of RSL in respect of its Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities since 9 October 2018 and Type 9 (asset management) regulated activity since 12 December 2018.

³ As at 29 May 2020, the Fund's NAV amounted to US\$94.5 million.

⁴ Investor A made a total of two subscriptions for the shares of the Fund in the aggregate amount of US\$90 million. The first subscription of US\$40 million was made in July 2019 and the second subscription of US\$50 million was made in April 2020.

purpose vehicle wholly owned by the Company (**SPV**) and guaranteed by the Company (**Senior Notes 1**).

8. According to the Purchase Agreement, RSL was one of the lead managers and joint bookrunners in the offering of Senior Notes 1 (**Offering**). RSL received a US\$120,000 fee from the SPV for its underwriting service provided in the Offering.
9. By purchasing Senior Notes 1 for the Fund on the one hand and underwriting the Offering and receiving the underwriting fee of US\$120,000 on the other hand, RSL placed itself in a conflict of interest situation. However, there is no evidence to show that RSL has taken reasonable steps to identify, prevent, manage and minimise the conflict arising from its underwriting activities and disclose the conflict to the Fund's investors.
10. It was only after the SFC raised concerns with RSL in October 2020 that RSL credited US\$120,000 to the Fund's account and disclosed the potential conflict of interest arising from its underwriting activities to the Fund's investors in December 2020.
11. RSL's conduct constitutes a breach of:
 - (a) paragraph 1.5 of the Fund Manager Code of Conduct (**FMCC**), which provides that a fund manager should maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to identify, prevent, manage and monitor any actual or potential conflicts of interest, and where an actual or potential conflict arises, the conflict should be managed and minimised by appropriate safeguards and measures to ensure fair treatment of fund investors, and any material interest or conflict should properly be disclosed to fund investors; and
 - (b) paragraph 10.1 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (**Code of Conduct**), which provides that where a licensed person has a material interest in a transaction with or for a client or a relationship which gives rise to an actual or potential conflict of interest in relation to the transaction, it should neither advise, nor deal in relation to the transaction unless it has disclosed that material interest or conflict to the client and has taken all reasonable steps to ensure fair treatment of the client.

A2. Failure to ensure the accuracy of a representation made on behalf of the Fund

12. On 21 April 2020, Investor A made a subscription for US\$50 million shares of the Fund.
13. On the same day, the Fund entered into a subscription agreement with the Company and the SPV (**Subscription Agreement**) to purchase US\$45 million of senior notes issued by the SPV and guaranteed by the Company (**Senior Notes 2**) through a private placement. The Subscription Agreement was signed by Fang on behalf of the Fund.

14. Two days later, on 23 April 2020, the Fund transferred US\$45 million of the US\$50 million subscription fee it had received from Investor A to the SPV's designated account to settle the purchase of Senior Notes 2.
 15. Among other things, the Subscription Agreement states that "*the [Fund] represents and warrants to [the SPV] and [the Company] that... the acquisition by it of [Senior Notes 2] is not and will not be financed directly or indirectly by any related party of [the SPV] or [the Company]...*" (**Representation**).
 16. The Representation was inaccurate as the source of funds used for purchasing Senior Notes 2 in fact came from Investor A, a related party of the Company and the SPV. At the material time, the Company, the SPV and Investor A were ultimately owned and controlled by the same individual, who also served as a chairman of all three companies.
 17. RSL has breached General Principle (**GP**) 2 of the Code of Conduct by failing to act with due skill, care and diligence to ensure the accuracy of the Representation made on behalf of the Fund in the Subscription Agreement.
- A3. Failure to have sufficient risk management measures to ensure the Fund was not exposed to excessive risk and ensure that its investment decisions were reasonable and in the Fund's best interests**
18. The SFC's investigation revealed that:
 - (a) Prior to November 2020, RSL did not set any specific limit to control and ensure the Fund's portfolio was not over-exposed to any single issuer.
 - (b) Although RSL had identified various downside factors and negative issues against the Company in its own analysis reports (such as the downgrading of the Company's credit rating, the liquidity problem faced by the Company and various internal problems of the Company, etc), it still decided to invest US\$45 million in Senior Notes 2 in April 2020, which together with the investment in Senior Notes 1 accounted for about 90% of the Fund's NAV⁵.
 - (c) Although Fang has provided an explanation for why he considered Senior Notes 2 to be worth investing in despite the downside factors and negative issues against the Company, RSL failed to justify why investing almost 90% of the Fund's NAV in one single issuer, ie, the SPV / the Company, was reasonable and in the Fund's best interest, considering the downside factors and negative issues against the Company.
 - (d) On 18 May 2020, RSL procured the Fund to purchase two bond-linked notes (**BLNs**) issued by a financial institution (**FI**), the performance of which was linked to Senior Notes 1. The Fund settled the purchase of the BLNs by selling Senior Notes 1 to the FI and paying an aggregate structuring fee of US\$47,562 to the FI⁶. According to RSL, it conducted the BLN transactions for the Fund in the hope that the price

⁵ Both Senior Notes 1 and Senior Notes 2 subsequently went into default.

⁶ On 23 July 2020, following the Company's default on one of its onshore bonds, RSL reached an agreement with the FI to unwind the BLNs and buy back Senior Notes 1 for the Fund.

of Senior Notes 1 might rebound in the future and the Fund might obtain additional liquidity by pledging the BLNs as collaterals. Fang claimed that he had discussed with the FI the idea of obtaining additional liquidity for the Fund through the BLNs.

(e) However:

- (i) As the BLNs and Senior Notes 1 have substantially the same risk and return profile, it is difficult to see any economic benefit for the Fund to exchange Senior Notes 1 for the BLNs at an additional cost.
- (ii) RSL was unable to explain why the BLNs, as compared with Senior Notes 1, would allow the Fund to obtain additional liquidity / financing more easily or at better terms.
- (iii) Further, according to the FI: (1) pursuant to the executed final terms of the BLNs, RSL / the Fund was not allowed to pledge the BLNs as collaterals for obtaining liquidity / financing without the FI's consent and (2) it had no knowledge of RSL's plan to obtain additional liquidity / financing for the Fund through the BLNs, and it did not provide any consent for RSL to pledge the BLNs as collaterals.

19. RSL has breached GP 2 of the Code of Conduct and paragraphs 1.2(d)⁷ and 1.7.1⁸ of the FMCC, by failing to (a) have sufficient risk management governance structure, policies and procedures to ensure the Fund was not exposed to excessive risk, and (b) ensure that its decisions to invest in Senior Notes 2 and the BLNs were reasonable and in the best interests of the Fund in light of all relevant factors at the material times.

A4. Failure to make adequate disclosure of information about the Fund's investment holdings

20. In May 2020, Investor A repeatedly requested RSL to disclose the Fund's top 10 investment holdings but such requests were rejected by RSL on the basis that RSL was "not supposed" to do so without the approval of all investors.

21. On 28 May 2020, Investor A emailed RSL that "*...For compliance purpose, can you please confirm if the [Fund] has invested in any bonds issued by [the Company] or any of its subsidiaries...*". On the same day, RSL replied to Investor A (**Reply**) that: "*[c]urrently, the Fund does not disclose relevant holdings to investors. However, considering that you are an important client to the Fund, please be informed that the Fund is holding multiple structured notes issued by investment bank(s).*"

⁷ Paragraph 1.2(d) of the FMCC requires a fund manager to maintain satisfactory risk management governance structure and procedures commensurate with the nature, size, complexity and risk profile of the firm and the investment strategy adopted by each of the funds under its management.

⁸ Paragraph 1.7.1 of the FMCC requires a fund manager to establish and maintain effective policies and procedures as well as a designated risk management function to identify and quantify the risks, whether financial or otherwise, to which the fund manager and, if applicable, the funds are exposed. The fund manager should take appropriate and timely action to contain and otherwise adequately manage such risks.

22. The Reply omitted the material fact that the Fund had invested about 90% of its NAV in fixed income products issued by or linked to the SPV / the Company.
23. It was only upon the SFC's request on 10 July 2020, ie, four days after the Company announced its default on its RMB1.5 billion onshore bond, that RSL disclosed to Investor A information about the Company-related investments held by the Fund.
24. By withholding the relevant information from Investor A, RSL has failed to make adequate disclosure of information about the Fund to and act in the best interest of Investor A, in breach of paragraph 6.2 of the FMCC⁹ and GP 2 of the Code of Conduct.

B. Deficiencies in RSL's account opening procedures

25. RSL launched a mobile application on 26 November 2018 through which Mainland residents could open an account with RSL on a non-face-to-face basis.
26. Before 1 August 2020, RSL engaged a Mainland service provider to provide certification services for client identity verification in respect of client accounts opened via RSL's mobile application. Further, RSL required every client to, upon completion of the account opening and identity verification procedures, transfer an initial deposit of not less than HK\$10,000 from a bank account in the client's name to RSL's bank account to activate the account within 30 days.
27. The identity verification procedures adopted by RSL as stated above were deficient, in that:
 - (a) the certifier engaged by RSL to provide certification services for client identity verification was not a recognised certification authority under the "Arrangement for Mutual Recognition of Electronic Signature Certificates issued by Hong Kong and Guangdong" and its electronic signature certificates did not obtain mutual recognition status accepted by the Government of the Hong Kong Special Administrative Region; and
 - (b) out of the 1,562 client accounts that were activated, 584 clients (ie, 37%) did not transfer an initial deposit of not less HK\$10,000 to RSL's bank account from a bank account in the client's name maintained with a licensed bank in Hong Kong.
28. RSL has breached paragraph 5.1 of the Code of Conduct¹⁰ by failing to adopt procedures in line with the acceptable account opening approaches set out in the SFC's website¹¹ for verifying the identities of clients who opened their

⁹ Paragraph 6.2 of the FMCC provides that where a fund manager is responsible for the overall operation of a fund, it should make adequate disclosure of information (as well as any material changes to the information) on the fund which is necessary for fund investors to be able to make an informed judgment about their investment into the fund.

¹⁰ Paragraph 5.1 of the Code of Conduct provides that where an account opening procedure other than a face-to-face approach is used, it should be one that satisfactorily ensures the identity of the client.

¹¹ For account opening in a non-face-to-face situation, the [SFC's website](#) sets out a list of approaches that are acceptable to the SFC, including (among others): (1) the use of certification services provided by

accounts through RSL's mobile application between 26 November 2018 and 31 July 2020.

Conclusion

29. Having considered all the circumstances, the SFC is of the view that RSL has been guilty of misconduct.
30. The SFC considers that RSL's failure in relation to its management of the Fund are attributable to Fang's failure to discharge his duties as an RO and a member of the senior management of RSL, in that he has failed to:
 - (a) act competently and diligently in carrying out the asset management activities on RSL's behalf; and
 - (b) ensure the maintenance of appropriate standards of conduct and adherence to proper procedures by RSL, in breach of GP 9 of the Code of Conduct¹² and paragraph 1.6(a) (Responsibilities of Management) of the FMCC¹³.
31. 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, including RSL's remedial actions, RSL and Fang's cooperation with the SFC in resolving the SFC's concerns and their otherwise clean disciplinary record.

certification authorities outside Hong Kong whose electronic signature certificates have obtained mutual recognition status accepted by the Hong Kong government; or (2) for online onboarding of clients, the carrying out of the following steps, including (among others), successfully transferring an initial deposit of not less than HK\$10,000 from a bank account in the client's name maintained with a licensed bank in Hong Kong (**Designated Bank Account**) to the intermediary's bank account and conducting all future deposits and withdrawals for the client's trading account through the Designated Bank Account only.

¹² GP 9 of the Code of Conduct provides that the senior management of a licensed person should bear primary responsibility for ensuring the maintenance of appropriate standards of conduct and adherence to proper procedures by the firm.

¹³ Paragraph 1.6(a) of the FMCC provides that the senior management of a fund manager should be principally responsible for compliance by the fund manager with all relevant legal and regulatory requirements, as well as the nurturing of a good compliance culture within the fund manager.