SFC revokes W. Falcon Asset Management (Asia) Limited's licence

4 Feb 2019

The Securities and Futures Commission (SFC) has revoked the licence of W. Falcon Asset Management (Asia) Limited (Falcon) for window-dressing its liquid capital, breaching the terms of a restriction notice and failing to provide timely notification of the resignation of its director who engineered the window-dressing scheme (Note 1).

The disciplinary action follows an SFC investigation which found that Falcon provided the SFC with false or misleading information in its licence application and financial returns between June 2014 and June 2017.

Falcon window-dressed its month-end liquid capital by including in its liquid capital computation the amount of certain cheques, which were subsequently dishonoured. This practice was adopted from the time of Falcon's SFC licence application. Had the amount of these cheques been excluded, Falcon would have been denied a licence to carry on regulated activities due to a liquid capital deficit at the time of its licence application and at each of the month-ends over a three-year period.

In May 2017, the director of Falcon guaranteed a loan taken out in the name of Falcon. Two months later, the SFC issued a restriction notice against Falcon after a self-report by Falcon that its liquid capital had dropped below the required level. Subsequently, Falcon defaulted on repayment of the loan and proceeded to enter into a debenture with the lender, thereby subjecting its assets to a floating charge, contrary to the terms of the restriction notice (Note 2).

The director resigned from Falcon on 23 October 2017, but both the director and Falcon failed to provide the SFC with written notification of such resignation within seven business days as required.

The SFC is of the view that Falcon's failures were in breach of the various regulatory provisions including the Code of Conduct. The failures also cast doubt on Falcon's ability to carry on regulated activities competently and call into question its fitness and properness to remain licensed by the SFC (Note 3).

In deciding the penalty, the SFC took into account all relevant circumstances of the case, including:

- the misconduct was egregious and serious;
- investors' and the public's confidence in market integrity was damaged;
- Falcon had an otherwise clean disciplinary record; and
- the need to remove Falcon from the industry in order to protect the investing public.

End

Notes:

1. Falcon was licensed to carry on Type 1 (dealing in securities), Type 4 (advising on securities) and Type 9 (asset management) regulated activities under the Securities and Futures Ordinance.
2. The restriction notice prohibited Falcon from carrying on all regulated activities, disposing of or dealing with any relevant property in any manner without the SFC's prior written consent, except for the return of any client money, client securities or any other client assets held by it as directed by the relevant clients. Please see the SFC's press release dated 7 July 2017.
3. Code of Conduct for Persons Licensed by or Registered with the SFC.

A copy of the Statement of Disciplinary Action is available on the SFC website

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STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has revoked the licence of W. Falcon Asset Management (Asia) Limited (**Falcon**) pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).

2. The disciplinary action is taken against Falcon for window-dressing its liquid capital, breaching the terms of a restriction notice issued against it (**RN**), and failing to notify the SFC of the resignation of one of its directors (**Director**) in a timely manner in contravention of sections 135, 146, 383 and 384 of the SFO and rules 6 and 55 of the Securities and Futures (Financial Resources) Rules (**FRR**).

Summary of facts

3. Falcon was granted a licence by the SFC to carry on Types 1, 4 and 9 regulated activities on 17 July 2014. Less than two months later, the Director became the sole owner of the entity which wholly owned Falcon.

4. The SFC found that Falcon has, during the period between June 2014 and June 2017, provided false or misleading information in its licence application and financial returns (**FRs**). It failed to maintain sufficient liquid capital and to notify the SFC of its inability to do so. Falcon also gave the SFC notice of the resignation of the Director who was the mastermind of the window-dressing scheme out of time.

5. In May 2017, the Director guaranteed a loan taken out in the name of Falcon (**Loan**). Shortly afterwards, the SFC issued the RN subsequent to which Falcon defaulted in repayment of the Loan. Falcon then entered into a debenture with the lender thereby subjecting its assets to a floating charge which was contrary to the terms of the RN.

6. Falcon had a practice of window-dressing its month-end liquid capital reported to the SFC. This was made possible by depositing cheques signed by the Director which were included in the bank balance amount of the relevant FRs which were in turn included in Falcon's liquid capital computation. However, such cheques were dishonoured upon presentation on the next business day. The practice had been adopted since the time of the application of Falcon's licence. If Falcon's liquid capital did not include the amount of the dishonoured cheques, it would have firstly, been denied a licence to carry on regulated activities; and secondly, had a liquid capital deficit on each of those month-end dates for 3 years from June 2014.

7. The RN which was issued on 7 July 2017 prohibited Falcon from carrying on all regulated activities, disposing of or dealing with any relevant property in any manner without the SFC's prior written consent, except for the return of any client money, client securities or any other client assets held by it as directed by the relevant clients. The SFC's decision followed a self-report by Falcon that its liquid capital had dropped below the amount required under the FRR. This

was uncovered as a result of an RO being notified of a dishonoured cheque issued by the Director in favour of Falcon.

8. The Director resigned from Falcon on 23 October 2017. However, the SFC only received Falcon's notification about the Director's resignation on 21 November 2017.

Breaches and reasons

Provision of false and misleading information in Falcon's licence application

9. Under section 383(1) of the SFO, a person commits an offence if he either makes a representation that is false or misleading in a material particular, or he knows that, or is reckless as to whether the representation is false or misleading in a material particular.

10. Falcon caused to be submitted to the SFC firstly, a "supplement 7 - financial resources" form stating it had excess liquid capital in the sum of HKD1.9 million, and secondly, a copy deposit slip showing that a cheque for the sum of HKD4 million was deposited on 30 June 2014. By doing so, Falcon held out that it had the requisite liquid capital to fulfil the requirements for qualifying for a licence.

11. In addition to the HKD4 million cheque, the supplement form also took into account another cheque in the sum of HKD990,000 in arriving at the figure of HKD1.9 million for excess capital. Both cheques were dishonoured upon presentation. In short, Falcon provided information in its licence application which was false and misleading.

Provision of false and misleading information in the FRs and failure to maintain sufficient liquid capital

12. Section 56(1) of the FRR requires a licensed corporation to submit to the SFC its FR in respect of each month end. The FR shall include, among other things, the month-end liquid capital computation of the licensed corporation. Under section 384(1) of the SFO, a person commits an offence if he, either in purported compliance with the SFO, provides to the SFC any information which is false or misleading in a material particular, or he knows that, or is reckless as to whether the information is false or misleading in a material particular. Under rule 6 of the FRR, a licensed corporation shall at all times maintain liquid capital which is not less than its required liquid capital. For Falcon, the required amount was HKD3 million.

13. Between 2014 and 2017, Falcon submitted a total of 28 FRs each containing a computed amount of liquid capital which purportedly exceeded the required minimum. According to the computation prepared by Falcon, the major component of its liquid capital was its "bank balance held in other accounts and cash in hand". Such bank balance amount included 38 cheques issued by the Director in favour of Falcon and were deposited at month end into its bank accounts.

14. All 38 cheques were dishonoured upon presentation. Had the amounts of such cheques been excluded from the computation, Falcon would have liquid capital deficit. Falcon therefore provided false and misleading information in the FRs and failed to maintain sufficient liquid capital.

Failure to notify the SFC of insufficient liquid capital

15. Section 146 of the SFO provides that if a licensed corporation becomes aware of its inability to maintain sufficient liquid capital, it shall notify the SFC in writing as soon as reasonably practicable. According to rule 55 of the FRR, a licensed corporation shall notify the SFC as soon as reasonably practicable and within one business day of it becoming aware of certain matters including its liquid capital had fallen below 120% of its required liquid capital and any information contained in any of its previous FRs had become false or misleading in a material particular.

16. Notwithstanding such requirements, Falcon failed to notify the SFC of either its inability to maintain liquid capital, its liquid capital had fallen below 120% of its required liquid capital, or the information contained in its FRs had become false or misleading in a material particular.

Failure to notify the SFC of cessation of a director

17. Section 135(6) of the SFO provides that where a person becomes or ceases to be a director of a licensed corporation, both the person and corporation shall provide the SFC with such notification together with certain details within 7 business days.

18. The SFC did not receive Falcon's notification about the Director's resignation until 20 days after which it was due.

Breach of the Code of Conduct

19. As a licensed corporation, Falcon is under a duty to act honestly, fairly, as well as with due skill, care and diligence, in the best interests of its clients and the integrity of the market under General Principles 1 and 2 (**GP**) of the Code of Conduct for Persons Licensed by or Registered with the SFC (**Code of Conduct**). According to GP 7, Falcon should comply with all regulatory requirements applicable to the conduct of its business activities so as to promote the best interests of clients and the integrity of the market. It should also comply with, and implement and maintain measures appropriate to ensuring compliance with the law, rules, regulations and codes administered or issued by, among other regulatory authorities, the SFC, pursuant to paragraph 12.1 of the Code of Conduct.

20. The above failures cast serious doubt on Falcon's ability to carry on regulated activities competently, honestly and fairly, and call into question its fitness and properness to remain licensed by the SFC.

Conclusion

21. Having considered all the circumstances, the SFC is of the view that Falcon is guilty of misconduct and is not fit and proper person to remain licensed.

22. The SFC has decided to revoke the licence of Falcon.

23. In deciding the disciplinary sanction against Falcon, the SFC has taken into account all the circumstances of this case, including:

- the misconduct was egregious and serious;

- investors' and the public's confidence in market integrity was damaged;
- Falcon had an otherwise clean disciplinary record; and
- the need to remove Falcon from the industry in order to protect the investing public.