STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has reprimanded Taiping Securities (HK) Co Limited (**TSCL**)[1] and fined it $1,300,000 pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).

2. The disciplinary action is taken in respect of TSCL's failure to: (a) communicate its personal dealing policy to all employees and ensure that they understood and followed the requirements therein, and (b) put in place adequate and effective internal controls over monitoring of employee dealings during the period between 1 January 2016 and 30 November 2018 (**Relevant Period**).

Summary of Facts

A. Failure to communicate its personal dealing policy to all employees and ensure that they understood and followed the requirements therein

3. TSCL claimed that its personal dealing policy contained in its Compliance Manual was updated in August 2014 and finalised in 2015, and was in force throughout the Relevant Period (**Personal Dealing Policy**)[2].

4. However, TSCL did not maintain any record to demonstrate that it had distributed the Personal Dealing Policy to all employees and clearly informed them that the policy was finalised and implemented during the Relevant Period. Nor did TSCL require its employees to sign any acknowledgement of receipt or understanding of the Personal Dealing Policy.

5. The Personal Dealing Policy provided that employees should not engage in speculative trading activities and day-trading is prohibited in principle. TSCL's definition of "*day-trading*" includes any one trade involving the buying and selling of the same stock within the same day (regardless of the amount and quantity involved), and the term "*prohibited in principle*" in the context of day-trading means that the activity was strictly prohibited save for extreme situations such as there being a "flash crash" in stock prices. TSCL claimed that it had communicated the definition of this requirement to its employees orally during daily communications and meetings.

6. Contrary to the above requirement, seven employees of TSCL had conducted day-trading (in accordance with TSCL's definition) during the Relevant Period. Four out of the seven employees claimed that the Personal Dealing Policy was not circulated to them or officially implemented during the Relevant Period, and most of them considered that TSCL did not prohibit day-trading generally but only those that were speculative in nature and where the employees did not have sufficient money in the account for trade settlement. Their views were reinforced by TSCL's lack of action against their trades over the years.

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[1] TSCL is licensed under the SFO to carry on Type 1 (dealing in securities) regulated activity.

[2] The term "Personal Dealing Policy" in this statement refers only to TSCL's personal dealing policy applicable during the Relevant Period but not their preceding versions.

7. Based on the above, the SFC concludes that TSCL has failed to communicate the Personal Dealing Policy to all employees and ensure that they understood and followed the requirements therein.

8. TSCL's failure in this regard constituted a breach of:

   (a) General Principle (**GP**) 2 (Diligence) of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (**Code of Conduct**) which requires a licensed person to act with due skill, care and diligence, in the best interests of its clients and the integrity of the market;

   (b) paragraph 12.2(a) (Employee dealings) of the Code of Conduct which requires a licensed person to have a policy which has been communicated to employees in writing on whether employees are permitted to deal or trade for their own accounts in securities, futures contracts or leveraged foreign exchange contracts;

   (c) paragraph 12.2(b)(i) (Employee dealings) of the Code of Conduct which stipulates that, in the event that employees of a licensed person are permitted to deal or trade for their own accounts in securities, futures contracts or leveraged foreign exchange contracts, the written policy should specify the conditions on which employees may deal for their own accounts; and

   (d) section III.2 (Personnel and training) of the Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the Securities and Futures Commission (**Internal Control Guidelines**) which requires a licensed person to ensure that all staff members and other persons performing services on its behalf are provided with adequate and up-to-date documentation regarding the firm's policies and procedures including those relating to internal controls and personal dealings.

B. Failure to put in place adequate and effective internal controls over monitoring of employee dealings

No written record of the review or monitoring performed on employee dealings

9. TSCL's employees were not required to obtain TSCL's pre-clearance before conducting trades in their personal accounts. TSCL's Settlement Department would prepare daily reports of all transactions in the employees' personal accounts with TSCL on a T+1 basis (**Daily Transaction Reports**) and pass them to TSCL's then Head of Dealing cum responsible officer (**RO**) for review and circulation to members of the General Manager's Office (**Senior Management**) for further review. According to the Personal Dealing Policy, the Compliance Department and the Senior Management were responsible for monitoring employee dealings.

10. However, TSCL did not maintain records of any reviews performed by the RO, the Senior Management and / or the Compliance Department on the Daily Transaction Reports, or any follow-up action taken by them in that regard. TSCL also did not have any written manuals, guidelines or procedures specifying how the review or monitoring of employees' transactions should be

performed, including the types of patterns or potential irregularities that had to be watched out for.

Personnel responsible for monitoring employee dealings did not have a clear and consistent understanding of their roles and duties

11. The Senior Management, the Compliance Department and the RO did not have a clear and consistent understanding of their respective roles and duties in monitoring employee dealings.

12. On the one hand, the RO considered that the Senior Management and the Compliance Department should be the ones responsible for reviewing the Daily Transaction Reports, while his role was merely to perform a preliminary review of the same.

13. On the other hand, the compliance officers of TSCL during the Relevant Period claimed that that they were not responsible for and did not carry out any review and / or monitoring of employee dealings. The Senior Management also did not consider it to be their responsibility to monitor employee dealings and claimed that the responsible officers, direct supervisors and the Compliance Department were instead responsible for monitoring employee dealings.

No independent review and approval of the RO's personal transactions

14. During the Relevant Period, the RO placed 814 trade orders in his personal account with TSCL, out of which 293 exceeded the trading limit prescribed by TSCL for his personal account (**Limit-Exceeding Transactions**).

15. The RO's personal transactions, including his Limit-Exceeding Transactions, during the Relevant Period were not subject to any independent review and approval:

    (a) TSCL claimed that its trading system was set to consider the trading limit, account balance and securities value of the relevant employee's account. When the system detected that the employee's order had exceeded the relevant account's limit, the order would be put on hold and not be executed unless the order was approved by a designated staff member.

    (b) However, the designated staff members responsible for approving Limit-Exceeding Transactions were the RO himself and a staff member who reported to him under TSCL's organisational hierarchy. TSCL did not require the designated staff members to document their reasoning when approving Limit-Exceeding Transactions.

    (c) The RO approved his own Limit-Exceeding Transactions on 160 instances and the reasoning behind each approval was not documented.

    (d) As stated above, the Senior Management and the Compliance Department did not perform any review or monitoring of the employees' transactions set out in the Daily Transactions Reports, including the RO's.

16. In light of the matters set out in paragraphs 9 to 15 above, the SFC is of the view that TSCL has failed to put in place adequate and effective internal controls over monitoring of employee dealings, in breach of:

(a) GP2 of the Code of Conduct;

(b) paragraph 4.3 (Internal control, financial and operational resources) of the Code of Conduct which requires a licensed person to have internal control procedures and financial and operational capabilities which can be reasonably expected to protect its operations, its clients and other licensed or registered persons from financial loss arising from theft, fraud, and other dishonest acts, professional misconduct or omissions;

(c) paragraph 12.2(b)(vi) of the Code of Conduct which requires transactions of employees' accounts and related accounts to be reported to and actively monitored by senior management of the licensed person who should not have any beneficial or other interest in the transactions and who should maintain procedures to detect irregularities and ensure that the handling by the licensed person of these transactions or orders is not prejudicial to the interests of the licensed person's other clients;

(d) section V.4 (Compliance) of the Internal Control Guidelines which requires a licensed person to establish, maintain and enforce effective compliance procedures, which should cover, amongst others, internal control matters and staff dealing requirements; and

(e) paragraph A4 of the Appendix to the Internal Control Guidelines which provides that the licensed person should put in place procedures to ensure that its staff's trading activities are not prejudicial to the interests of its clients and all transactions for staff accounts are separately recorded and diligently monitored by independent senior management.

Conclusion

17. Having considered all the circumstances, the SFC is of the opinion that TSCL is guilty of misconduct.

18. In deciding the disciplinary sanction set out in paragraph 1 above, the SFC has taken into account all of the circumstances, including TSCL's remedial measures to enhance its internal systems and controls on employee dealings and its otherwise clean disciplinary record.