

# SFC Reprimands and Fines Guotai Junan Securities (Hong Kong) Limited for Breaches of the Financial Resources Rules and the Client Money Rules and Other Internal Control Failures

8 Sep 2005

The SFC has reprimanded Guotai Junan Securities (Hong Kong) Limited and fined it \$400,000 for failing to maintain the required liquid capital and to deposit client money with authorised financial institutions. Guotai Junan also had other internal control problems which were subsequently rectified (Note 1). The reprimand and fine are the result of a settlement between Guotai Junan and the SFC. The SFC considers the settlement to be in the public interest and in the interests of investors.

In October 2003, Guotai Junan took out bank loans to finance clients' applications for the IPO of PICC Property and Casualty Company Limited. The amount lent to its clients had an effect on the statutory liquid capital requirement and Guotai Junan overlooked the effect. As a result, Guotai Junan's liquid capital fell below the statutory requirement by \$55 million on 30 October 2003. The deficit was rectified afterwards.

The SFC also found that, between December 2002 and November 2003, Guotai Junan inadvertently deposited client money with three overseas banks that were not authorised financial institutions under the Banking Ordinance, hence breaching the Client Money Rules. Further, the deposits with two banks had to be treated as ranking liabilities under the Financial Resources Rules (FRR), which caused deficits in the required liquid capital from March to October 2003. The funds held with such overseas banks were ultimately maintained in bank accounts in authorised financial institutions in Hong Kong. Those funds were withdrawn by Guotai Junan as soon as practicable once the breaches were identified. Guotai Junan also strengthened its internal control procedures to prevent the recurrence of such inadvertent errors.

The SFC further identified other minor internal control problems at Guotai Junan. However, the SFC notes that Guotai Junan has since rectified these problems and strengthened its internal control procedures to prevent the recurrence of such problems.

The SFC concludes that Guotai Junan has been guilty of misconduct and that its fitness and properness has been called into question. In deciding on the penalty, the SFC has taken into account the Disciplinary Fining Guidelines (Note 2) and all the circumstances of the case, including the following:

- (i) all of the breaches were unintentional;
- (ii) Guotai Junan had taken remedial action and had strengthened its internal control system to prevent recurrence of the breaches;
- (iii) no loss or damage was suffered by clients, market users or the general public;
- (iv) Guotai Junan made extra profits as a result of the overseas deposits and the excessive margin lending;
- (v) Guotai Junan promptly reported the FRR breaches to the SFC in accordance with section 146 of the Securities and Futures Ordinance;
- (vi) Guotai Junan had at that time sufficient resources to finance its business operation;
- (vii) Guotai Junan has co-operated with the SFC throughout the SFC's investigations.

Mr Alan Linning, SFC's Executive Director of Enforcement, said: "Compliance with the FRR and the Client Money Rules affords protection to the investing public. The breach of these rules could seriously undermine the financial integrity of a broker. Licensed corporations should have adequate internal controls to protect the integrity of their business operations and their clients' interests. This is vital to investors' confidence in Hong Kong's securities and futures markets."

Ends

Notes to Editors:

1. Guotai Junan is a corporation licensed under the Securities and Futures Ordinance to carry on business in Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities.
2. The SFC issued the [Disciplinary Fining Guidelines](#) in March 2003 under section 199(1)(a) of the Securities and Futures Ordinance.

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